Kentucky Public Pension Work Group
County Employee Retirement System

FINAL REPORT:
10/30/08

State Auditor of Public Accounts Crit Luallen, Chair
Senior Policy Advisor Joe Meyer, Co-Chair

Subcommittee Staff
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Public Pension Working Group
County Employee Retirement System Subcommittee
October 28, 2008

Executive Summary

Subcommittee Purpose:

- Study the potential transfer of classified school board employees and retirees currently in the County Employees Retirement System to the Kentucky Teachers' Retirement System (KTRS), the Kentucky Employee Retirement System (KERS) or leave them in the CERS and rate them separately from city/county employees, or move local government employees to a new retirement system, to be known as the Local Government Employees Retirement System.

Core Issue:

- Are non-school board members subsidizing school board members in CERS? If so, what subsidy exists and how do you deal with the actuarial and operational consequences? Is there a counter-balancing subsidy through the provision of health care benefits to local government retirees whose employers do not participate in the Kentucky Employees Health Plan (KEHP)?

Key Findings:

- When rated separately: Non-School Board employees actually receive a small subsidy from school board employers on pension contributions but School Boards receive a larger subsidy from non-school board employers on the health insurance contributions.
- Cavanaugh MacDonald, KRS actuarial consultants, found that non-school board employers subsidize school board employers in an amount that ranges from $32.6 million to $43.8 million, depending on the assumptions used. PricewaterhouseCoopers found that local government employers who do not participate in KEHP benefit from a $37.2 million subsidy for their "unescorted retirees".
- If the groups in CERS were divided, over time, school boards would pay approximately 3% more than the current employer rate; non-school boards would pay approximately 5% less than the current employer rate.
- Any action to rate classified school board employees separately from city and county employees should be done in the first year of a biennium to allow for adequate consideration in the Executive Branch Budget. Transferring employees in an odd-numbered year will result in school boards being required to absorb higher annual required contributions without a structural means of including that expenditure in their budget.

- The CERS Subcommittee identified five possible courses of action to address the question raised in the Executive Order. Any action that would separate the school board employees from the non-school board employees would cost the retirement systems millions of dollars in extra administrative costs.

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INTRODUCTION

Governor Steven L. Beshear established the Public Pension Working Group by signing Executive Order 2008-460 on May 29, 2008. The Public Pension Working Group (PPWG) was tasked to study certain issues related to pension reform and provide a report to the Governor on or before November 1, 2008. In order to facilitate this task, the PPWG was organized into six subcommittees, each providing input on specific topics.

The County Employee Retirement System (CERS) subcommittee was formed to study two issues: moving classified school board employees from CERS to a different system (Kentucky Teachers Retirement System); and establishing a Local Government Employee Retirement System (LGERS) to manage city and county employee retirements. The pertinent language from Executive Order 2008-460 is stated below.

- Studying the creation of a new retirement system, to be known as the Local Government Employees Retirement System. Membership in the Local Government Employees Retirement System would consist of employees, employers, and retirees of agencies participating in the County Employees Retirement System who are not school boards as defined by KRS 78.510(4);

- Studying the potential transfer of classified school board employees and retirees currently participating in the County Employees Retirement System to the Kentucky Teachers' Retirement System, while ensuring that in the event that such transfer occurs, the classified school board employees who become members of the County Employees Retirement System on or after July 1, 2008 shall be provided with the same benefits provided to classified school board employees who become members of the Kentucky Teachers' Retirement System on or after the date of the transfer to the Kentucky Teachers' Retirement System.

At the initial meeting, CERS subcommittee members agreed that the scope of work should be modified to include a review of the following options for classified school board employees—moving them to Kentucky Teachers' Retirement System (KTRS), transferring them to Kentucky Employees Retirement System (KERS), or leaving them in County Employees Retirement System (CERS) and rating them separately from city/county employees. While the executive order excluded the KERS and separate rating in CERS options, the subcommittee report will address all the potential alternatives.

Membership of the Subcommittee included representatives of the Kentucky Education Association, Kentucky League of Cities, Kentucky Association of Counties, Kentucky Association of School Superintendents, Kentucky School Boards Association and Kentucky Association of School Administrators, Fraternal Order of Police, Kentucky Firefighters Association, Kentucky Professional Firefighters and Kentucky Association of State Employees. A full listing of membership is marked Appendix I.

SUMMARY OF MEETINGS

The Subcommittee held public meetings on July 22nd, and August 18, 2008 with the following results:

- Approved the actuarial firm of Cavanaugh Macdonald, to conduct a CERS Reorganization Study to determine if any subsidy exists in favor of one group and if a division were to occur how the assets would be divided.

- Testimony was received by interested parties. These groups included Kentucky Retirement System, Kentucky Education Association, Kentucky League of Cities, Kentucky Association of County Officials, Kentucky Association of School Superintendents, School Boards and School Administrations, Fraternal Order of Police, Kentucky Firefighters Association, Kentucky Association of State Employees, Kentucky Teachers Retirement and PricewaterhouseCoopers. Written testimony is included in the report as Appendix II. All parties were in agreement that an actuarial study was needed to accurately address the issues.

On September 25, 2008 a third meeting was held. Cavanaugh Macdonald presented their findings, the results of which are presented later in this report.

PricewaterhouseCoopers, consultants to the Personnel Cabinet, also presented a report entitled, "The Impact of Unescorted Retirees" An Actuarial Analyses, dated September 24, 2008. Kentucky League of Cites and Kentucky Association of County Officials requested a meeting with PricewaterhouseCoopers to analyze specific questions. The revised PricewaterhouseCoopers report dated, October 17, 2008, is discussed later in this report.

BACKGROUND – CERS STRUCTURE

The Kentucky Retirement System (KRS) manages three independent retirement programs: the Kentucky Employees Retirement System for employees of state government; the County Employees Retirement System (CERS) for employees of local governments; and the State Police Retirement Systems (SPRS). Each program has a different retirement benefit structure.

The County Employees Retirement System (CERS) currently includes just over 180,000 members as of June 30, 2008, distributed as shown below:

	Classified School Board Employees	City and County Employees	Total
Active Members	50,620 (57.3%)	36,569 (42.7%)	87,189
Inactive Members			
Vested	4,869 (57.6%)	3,661 (42.4%)	8,530
Non-vested	29,185 62.1%)	18,227 (39.9%)	47,412
Retirees/Beneficiary	19,766 (53.7%)	17,293 (46.3%)	37,059
Total	104,440 (57.8%)	75,750 (42.2%)	180,190

In addition to a pension benefit, KRS provides health insurance benefits for all CERS retirees according to their age and years of service. All retirees who are Medicare eligible (age 65 and over) are covered under the Medicare supplement plan that is self-insured/self-administered by KRS. Retirees who are under the age of 65 are insured through the Kentucky Employees Health Plan (KEHP) along with all active employees of participating agencies. KRS pays the appropriate insurance premium to KEHP on behalf of the retiree. This is true regardless of whether or not the retiree was insured in the KEHP as an active employee. Any retiree that did not participate in KEHP during his or her active service has been classified as an "unescorted retiree" by administrators of that plan.

The insurance premium paid by KRS is the same for every retiree within the same benefit plan (hazardous or non-hazardous) and the same years of service—it is a percentage of premium or a level dollar amount and not related in any way to the compensation of the employee; i.e., lower paid employees receive the same health benefit as those with much higher salaries, provided they have the same number of years of service.

During an employee's active service, employers provide a monthly contribution to KRS for the purpose of pre-funding the retiree's pension benefit and health insurance coverage. The KRS Board of Trustees calculates the employers' Annual Required Contribution (ARC) as a percentage of payroll, and employers participating in CERS are required to pay the calculated amount. Employers will make smaller contributions on behalf of lower paid employees than for those with higher salaries.

At Issue: Dueling Health Care Subsidies: KEHP Unescorted Retirees v. CERS Retiree Health Care Costs

The basic question of removing school board employees from CERS first surfaced in October 2001. The Group Health Insurance Board that oversees KEHP issued an annual report that stated the unescorted retirees added $10 million to the total cost of KEHP health care for fiscal year 2000. Subsequent annual reports contained updated costs of unescorted retirees through fiscal year 2003, when the reported amount had increased $21 million.

In 2002, the Personnel Cabinet, as administrators of KEHP, requested legislative relief from the financial burden of unescorted retirees. They drafted language that would require all agencies with non-Medicare eligible retirees to either participate in KEHP for active employees or pay the actuarial cost difference for their unescorted retirees. The bill did not pass in its original form. Instead, the legislature required the Interim Joint Committee on State Government to study the issue and report results by November 1, 2003. The Legislative Research Commission (LRC) retained Segal and Associates to conduct an actuarial analysis of additional costs for unescorted retirees. According to Segal, unescorted retirees added $14.1 million to KEHP expenditures in fiscal year 2001.

Concurrent with the LRC study, the KRS actuary, Mercer Human Resources Consulting, was asked to determine if city and county employers may be incurring additional costs to subsidize school board employees through their annual required contribution paid to KRS for retiree health insurance. Due to the fact that city and county employees normally have much higher salaries than classified school board employees, it was suspected that cities and counties could be paying more total dollars for retiree health care than their school board counterparts.

Mercer determined that city and county employees comprised only 42% of the total membership of CERS but accounted for 59% of the gross reported salaries. Assuming that all demographic factors of city and county employees were identical to classified school board employees (mortality rate, turnover rate, retirement rate, etc), Mercer determined that city and county employers could have saved $13.8 million in fiscal year 2001 had they been rated separately from school board employers. The $13.8 million additional cost to the city and county employers basically offset the $14.1 million additional cost of the city and county unescorted retirees to the KEHP plan.

In the 2003 Regular Session of the General Assembly, HB 103 included a compromise between city and county governments and school boards designed to address the unescorted retiree issue.

A floor amendment to the bill required that cities and counties pay the actuarial amount of the unescorted retirees to KEHP, and the Department of Education was to seek a General Fund appropriation to cover the subsidy that city and county governments were paying to KRS to the benefit of classified school board employees. The bill did not pass in 2003. A similar proposal stalled again as HB 11 in the 2004 Regular Session. No further legislative action was taken until the 2008 Regular Session, when HB 600 SCS included language from the Senate to establish LGERS and move classified school board employees to KERS. . The LGERS/classified school board employee issue was a major point of disagreement during the final negotiations on HB 600. In order to resolve this issue, the Governor specifically tasked the PPWG to study the problem and provide alternatives.

SUBCOMMITTEE APPROACH/METHODOLOGY

In the first meeting, CERS subcommittee members agreed to a full actuarial analysis of CERS to determine what, if any, subsidy exists. While the studies done by both Segal and Mercer were comparable because both studies assumed identical demographics for CERS' total membership, it was possible that significant differences could have existed between classified school board and city and county employees, which would mean that these past studies were less than totally accurate. Ohio and Missouri both have separate systems for classified school boards, and experience studies indicate significant differences in withdrawal (termination) rates, retirement rates and mortality rates. The CERS subcommittee agreed to use the services of Cavanaugh Macdonald, LLC, to conduct an up-to-date, comprehensive analysis. Cavanaugh Macdonald is also under contract to provide actuarial services to both KRS and KTRS.

On July 22, 2008, Tom Cavanaugh, CEO of Cavanaugh Macdonald, briefed the committee on the approach to be taken.

- Conduct independent experience studies of School Board and Non-School Board Employees.

- Determine if different actuarial assumptions apply to the two groups.

- Apply the appropriate assumptions to the two groups and perform calculations to determine whether a subsidy exists, and in which direction.

- If a material subsidy exists, determine methodology for dividing the assets and provide a 20-year projection of the two systems separately to determine the impact on employer contribution rates.

SUMMARY OF RESULTS

A full copy of the Cavanaugh Macdonald report is marked Appendix III. Summary results are presented as follows:

- CERS School Board employees do have different actuarial demographics than Non-School Board Employees. School Board Employees:
  - ➢ Terminate earlier;
  - ➢ Retire later;
  - ➢ Have a different mortality rate; and
  - ➢ Have significantly lower average salaries. ($17,592 versus $33,662 for NSB)

- When rated separately:
  - ➢ Non-School Board employees actually receive a small subsidy from school board employers on pension contributions.
  - ➢ School Boards receive a larger subsidy from non-school board employers on the health insurance contributions

Cavanaugh MacDonald found that using the assumptions used in the 2007 actuarial valuation and the full ARC for 2008, the subsidy in favor of the school boards is $43,775,319. It should be noted that CERS employers did not pay the full ARC in 2008 as the KRS board had approved a five year phase-in of the higher ARC resulting from the implementation of GASB 43/45 accounting rules. The use of the actual ARC would result in a different subsidy amount.

Using the new assumptions based on the experience study for the school board/non-school board employees, Cavanaugh MacDonald found a subsidy of approximately $32.6 million. Cavanaugh MacDonald opined that "…long term, the new assumptions will reflect the differences between the groups better than the current assumptions do." Because the discussion to date has been about the current subsidy, not the long term subsidy, Cavanaugh MacDonald has emphasized the current subsidy amount.

- If the groups were divided, over time –
  - ➢ School boards would pay approximately 3% more than the current employer rate.
  - ➢ Non-school boards would pay approximately 5% less than the current employer rate.

OPTIONS

At the outset, the analysis of this subcommittee was done independent of and without regard to the impact of the subsidy that exists for unescorted retirees in KEHP. However, before reaching a final decision to reorganize CERS, the subsidy for unescorted retirees should be compared to the subsidy for pension and health insurance in KRS. Any counterbalancing effect should be considered in drafting future legislation.

The Cavanaugh Macdonald Report found that non-school board employers subsidize school board employers in an amount that ranges from $32.6 million to $43.8 million, depending on the assumptions used. The PricewaterhouseCoopers Report commissioned by the Personnel Cabinet entitled, "The Impact of Unescorted Retirees" An Actuarial Analysis (dated October 17, 2008) shows a subsidy of $37.2 million for unescorted retirees, Appendix IV. The PricewaterhouseCoopers study has incorporated to the extent possible recommendations from the Kentucky League of Cities of affected agencies.

General Discussion of Options

CERS participants have a benefit structure different from that of either KERS or KTRS participants. The CERS annual multiplier, for example, differs from KERS; CERS participants have an inviolable contract for health insurance benefits; KTRS employees do not. Because of these differences it will be impossible to blend school board employees into another group to mitigate the employers' actuarial contributions.

The school board members can be rated separately from the non-school board members, regardless of placement. Under separate rating, the costs attributable to school board employees can be separately identified and assigned to their employers.

Any action to rate classified school board employees separately from city and county employees should be done in the first year of a biennium to allow for adequate consideration in the Executive Branch Budget. Transferring employees in an odd-numbered year will result in school boards being required to absorb higher annual required contributions without a structural means of including that expenditure in their budget.

If school board employees are to be rated separately from city and county employees, the only alternative is to divide both the membership and the assets into two separate groups, regardless of the governance structure.

The following actions must be completed to rate the groups separately:

- Divide the assets

  - Actuary will use the actuarial accrued liability of the two groups as measured by an experience study
  - Cover retiree liability and accumulated active member contributions at 100%
  - Divide the remaining assets by the ratio of active member accrued liability
  - Update the asset liability models for each new fund to determine whether any changes should be made in asset allocation – approximately $50,000 per study

There is a difference between the actuarial value of assets and the market value. The actuarial value reflects a smoothing adjustment, meant to reduce the volatility of market changes. If a split of assets were to occur, the split would be based on actual market value as of the date of the split. In the current economic circumstances the market value is less than the actuarial value, which would cause the contribution rates for both groups to increase.

- Divide the membership

  - All 154,000 member records of active and inactive CERS members must be manually audited to ensure the proper service credit is determined for each employee and benefits are paid from the appropriate fund upon retirement. KRS' costs would be considerable given the complexity and is estimated at one million dollars per year for five years.

  - Once the manual audit of membership status is complete, the actuary would need to review the results and recalculate the actual division of assets and "level" the calculations if there are any differences from the original experience study

  - Minimum time to accomplish all actions: 48 months

The CERS Subcommittee identified five possible courses of action to address the question raised in the Executive Order:

Option 1: Leave system "as is"

Under this option, the parties would recognize that the subsidy on the pension/health insurance contributions in CERS would be somewhat offset by the subsidy for unescorted city/county retirees. As the subsidies are comparable, there is little incentive to incur the disruptions.

Option 2: Leave school board employees and local government employees in CERS: Rate each group separately.

- Maintain both groups under the CERS structure and create a subset for school board employees. The separate school board pension and health trust funds would be similar to the CERS Hazardous subset now in existence
- Membership and assets would be split
- Trust funds would not have to be moved to another governance structure
- Least complicated option to implement
- Would increase costs paid by school boards
- Would decrease costs paid by non-school board employers

Option 3: Move school board employees to KTRS; Leave local government employees in CERS

- CERS Membership and assets would be split

- CERS assets allocated to school board members would be moved to KTRS;
  - Changing securities from KRS to KTRS will take several months to mitigate market fluctuations
    - KRS and KTRS have different asset allocations, making securities transfer more difficult
    - Both KRS and KTRS will be required to do major rebalancing of funds during/after asset transfer
    - Some securities may have to be sold and equity reinvested

- KTRS would implement major management adjustments
  - Computer systems must be modified to accommodate the new members, transfer of service credit, assets, etc.
  - KTRS will have to hire and train additional staff – estimate of at least 35-40 full time employees.
  - KTRS will have to expand its equipment and office space requirements
  - Total time to prepare for transfer of employees and assets – 18-24 months

- KRS will have to make major staff adjustments once transfer of membership is complete

- Would increase costs paid by school boards

- Would decrease costs paid by non-school board employers

Option 4: Move school board employees to KERS; Leave local government employees in CERS

- CERS Membership and assets would be split

- Separate school board pension and trust funds would be transferred to KERS
  - Since funds are being moved within KRS umbrella, minimal impact to IRS regulations, etc.

- May consider adding school board-specific and/or city/county-specific representative to existing board or establishing advisory groups for each group of employees that would meet with the Board of Trustees on a regular basis

- Second least complicated option to implement

- Would increase costs paid by school boards

- Would decrease costs paid by non-school board employers

Option 5: Leave school board employees in CERS; Move City/County employees to the newly established LGERS

Establish a separate LGERS Board of Trustees to govern city/county plans

- Membership and assets would be split
- Statutory changes required to establish new board, membership, duties and responsibilities
- Determine if current KRS administrative staff will support both KRS and LGERS, or if LGERS will require its own staff structure
- Additional staff will be needed to support a second board even if LGERS shares administrative staff with KRS
- Draft bylaws and regulations to govern LGERS board functions
- All annual financial and actuarial reports will be duplicated—separate set required for LGERS, including:
  - Comprehensive Annual Financial Report (CAFR)
  - Annual Actuarial Analysis
  - Annual Investment reports
  - Actuarial experience studies
  - Audited Financial Statement and Independent Auditor's Reports

- Securities will have to be moved from KRS to LGERS

- IRS regulations govern "carving out" assets – will need fiduciary counsel involvement
- Securities must be transferred over a period of months to mitigate impact of market fluctuations
- Most complicated option to implement

If there is a decision to split the CERS groups, the Cavanaugh Macdonald Report states "Given that School Board members will be valued separately after the split, the most efficient choice is CERS." The staff of KRS agrees that this is the least complicated and least expensive choice. The legal firm of Ice Miller has provided an analysis of the IRS and fiduciary considerations to be considered if CERS assets are actually divided. Ice Miller is the KRS legal counsel for tax and fiduciary issues. A copy of the report is included as Appendix V.

The subcommittee recognizes that the fiscal impact on school boards will be significant if classified school board employees are rated separately from other employees in CERS. Policy makers will need to determine how to address this increased burden within the context of budget deliberations.

The implementation costs to KRS and/or KTRS must also be considered. KRS estimates a cost of approximately $5 million over five years to separate the CERS groups. KTRS estimates a start-up cost of $2.1 million and an annual cost of $3.4 million if school board members are moved to KTRS. Details are included in Appendix VI.

Reponses to the draft report from interested parties are included as Appendix VII.

Appendix I

Membership List

CERS/LGERS Subcommittee Membership

Chair: State Auditor Crit Luallen

Co-Chair: Senior Policy Advisor Joe Meyer

1) Arnold, Bob
   Executive Director
   Ky Assn. of Counties

2) Baird, David
   Executive Director
   Ky School Boards Assn.

3) Blankenship, Mary Ann
   Executive Director
   Ky Education Assn.

4) Bohman, Craig T.
   NKY Area Development District;
   Municipal Gov't League of NKY

5) Botkin, Doug
   Ky Education Assn.
   (Fayette Co. Classified Employee)

6) Burnside, Mike
   Executive Director
   Ky Retirement Systems

7) Caldwell, Glenn
   Mayor
   President Ky League of Cities,
   Mayor of Williamstown

8) Chaney, Colleen
   Secretary of State's Office

9) Representative Mike Cherry,
   House of Representatives Designee

10) Clark, Shirley
    Executive Director
    Ky Retired State Employees

11) Davenport, Richard
    KEA (Anderson Co. Bus Driver)

12) Davis, Edwin
    Ky Fraternal Order of Police

13) Dunagan, Daryl
    Ky Teachers' Retirement System

14) Gilmore, Stephen
    Superintendent of Ashland
    Independent. Schools;
    Former Mayor of Ashland

15) Hamberg, Jim
    Mayor
    Mayor of Southgate

16) Harbin, Gary
    Executive Director
    Ky Teachers' Retirement System

17) Ishmael, Kayne
    Ky Education Assn.

18) Jackson, Lee
    President
    Ky Assn. of State Employees

19) Jackson-Eaglin, Paula
    Ky Assn. of Professional Educators

20) Jenkins, David
    Judge
    Spencer Co. Judge Executive

21) Kurtsinger, Howdy
    Division Director
    Ky Fire Commission

22) Lampe, Stanford
    N.Ky Chamber of Commerce

23) Lang, Vince
    Executive Director
    Ky Co. Judge/Executive Assn.

24) Lovely, Sylvia
    Executive Director
    Ky League of Cities

25) McKim, Brent
    President
    Jefferson Co. Teacher's Assn.

Appendix II

Written Testimony During Meetings

Kentucky Fraternal Order of Police

Kentucky Association of State Employees

Kentucky Fire Fighters

3KT

Kentucky League of Cities

Kentucky Education Association

Kentucky Teachers' Retirement System

Kentucky Retirement System

Thank you madam chairman for allowing the Kentucky State Fraternal Order of Police to address the committee. We are not going to be as enthusiastic as the League of Cities was at the last meeting. We strongly oppose the L.G. E.R.S. that's being considered before this committee. Three (3) components make up the Kentucky Retirement System the only component that is financially sound is C.E.R.S. A financially sound unit of the Kentucky Retirement System should not be tampered with. The C.E.R.S. system is funded at 85% of the recommended funding and has sound management and investments. We feel that any attempt to split the system into two separate parts only makes both parts weak. The Retirement System testified last meeting that long term investments would have to be sold and divided to accomplish this split. This is not a wise decision especially now that the current economy is facing financial problems. This was only some of the problems outlined by the Retirement System regarding breaking up C.E.R.S into two separate systems.

We are also opposed to changing the make up of the current Retirement Board. We feel that the current board works well and change would not be the best for the entire system. We base this opinion on the fact that under House Bill #1 passed in the recent special session the League of Cities and KACO both agreed to take a (1) year payment holiday and pay a 29% contribution rate to the Kentucky Retirement System even though the rate is actually recommended to be much higher. The current employees that also pay a portion of their salary into the Retirement System didn't get to take a payment holiday nor did they ask to be given this option.

We feel that this is irresponsible on the part of Cities and Counties and certainly doesn't need to be rewarded with a seat on the Kentucky Retirement Board now or anytime in the future. We understand that their rates are high and places a financial strain on the Cities and Counties paying the rate. The rate is however, not higher than their obligation that is owed to their current and retired employees. This obligation should come before any special projects that the Cities or Counties might have. They do have the option of raising taxes if necessary. The only option that current employees have is just keep paying what's required of them. Cities and Counties are going to have a substantial saving from House Bill #1 on new employees hired after September 1 of this year.

We also oppose the removal of the classified employees from the C.E.R.S. system this seems to be an idea that has no good options. Fully funding the Classified Employees would be a better idea. This way the C.E.R.S. would remain strong and able to meet its obligations in the years to come.

CERS Reorganization

Crit Luallen, Chair
08-18-08

Madam Chair:

My name is Lee Jackson, President Kentucky Association of State Employees (KASE).

I just have a very brief statement regarding the potential transfer of classified school board employees and retirees currently participating in the County Employees Retirement System (CERS) to the Kentucky Teachers' Retirement System (KTRS).

As you are aware, this is a very complicated and controversial issue. Because of the complexities associated with this issue, it is our position that a comprehensive study and actuarial analysis should conducted before a decision is made whether to move employees and retirees from CERS to KTRS. We believe that all the facts should be on the table and that after all the facts are on the table; there should be in-depth discussion. Once the information has been fully vetted, a prudent decision can be made.

Thank you and the sub-committee for the opportunity to provide this input.

Local Government Employees Retirement System Board of Trustee (LGERS)

I want to thank you for the opportunity to address the subcommittee on the creations of the LGERS board of trustees. I represent the entire fire service today with the authority to speak for the following; Kentucky Fire Commission, Kentucky Firefighters Association, Kentucky Fire Chiefs Association and the Kentucky Professional Fire Fighter. On behalf of the entire fire service we do not support the creation of a LEGERS board because there are many unanswered questions. With the recent special session and the resultant positive changes that are expected to impact the CERS Hazardous Pension System we raise the following questions:

Many Unanswered Questions for LGERS:

* Will LGERS insure that Hazardous employers and employees unique actuarial requirements for health care are managed adequately?

* Serious questions remain regarding the dollar for dollar application of these funds to the hazardous employee's actual health care.

* Currently local governments are required to fully fund the actuarially required contribution (ARC). Will the creation of LGERS result in an employer dominated board that would adopt assumptions that are unrealistic and underfunding the system in order to save money during tight budget times?

* What would be the effect of dividing the plans assets if classified employees are moved to another plan? We express huge concerns of this move and its effects on future assets.

* Will the make-up of the proposed LGERS system insure that adequate representation is provided to the employee as well as the employer? The information I received from the League of Cities of the proposed structure demonstrates the employer dominated board (copy attached).

*We believe the creation of this board could cause the following:

- Unnecessary administrative burden
- Unnecessary duplication of services
- Cost millions

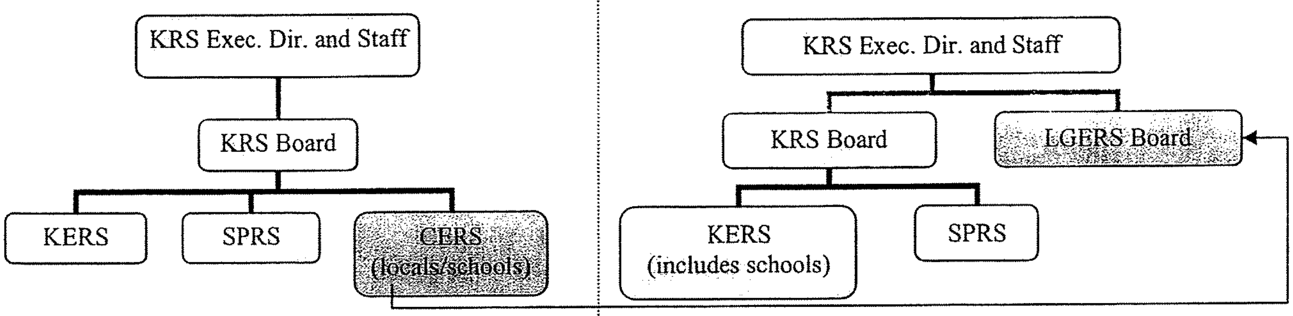
Other Important Facts

* The current CERS "Hazardous" pension system is funded at nearly 85%, approaching the national standard for a sufficiently funded system.

* The largest share of the employer's contribution to the Hazardous system is intended to pre-fund the retired employee's health care.

Local Government Employees Retirement System Board of Trustees

Current Structure | **Proposed Structure**



Membership

3 – Trustees appointed by Governor from a list of nine from the Kentucky League of Cities
3 – Trustees appointed by Governor from a list of nine from the Kentucky Association of Counties
2 – Trustees selected by nonhazardous duty membership
\+ 1 – Trustees selected by hazardous duty membership
9 – **Total trustees, one elected as chairperson by Board**

Powers

- Sue and be sued
- Conduct business and make bylaws
- Contract for professional services
- Purchase fiduciary liability insurance
- Manage goods or property
- Reimburse trustees for necessary expenses

Duties

- Promulgate administrative regulations
- Publish an annual financial report and audit
- Conduct an annual actuarial valuation
- Invest and reinvest funds
- Set annual employer contribution rates
- Determine individual hazardous duty coverage eligibility
- Establish distribution options for annuity savings accounts
- Determine benefits payable when disputed

Administration

Over 30 matters are administered in the same manner as provided for the Kentucky Employees Retirement Systems including but not limited to the following:

- Credit for prior service
- Cessation of membership
- Reinstatement
- Beneficiary designations
- Purchase of service
- Death and disability benefits

All benefits included in the Senate committee substitute constitute an inviolable contract of the Commonwealth except for those employees hired on or after July 1, 2008. The substitute does not affect contribution rates or benefits for current employees. A minimum 1.5 percent COLA is guaranteed for members who retire between July 1, 2009, and July 1, 2018.

3KT testimony to the CERS Reorganization Subcommittee

July 22, 2008

Good morning. My name is Dr. Leon Mooneyhan and I am the chief executive officer of the Ohio Valley Educational Cooperative, located in Shelbyville. I'm here on behalf of the 3KT organization, a partnership of the Kentucky Association of School Administrators, Kentucky Association of School Superintendents and Kentucky School Boards Association. I'm pleased to introduce to the committee my colleagues: Bill Scott, Executive Director, Kentucky School Boards Association; Wayne Young, Executive Director, Kentucky Association of School Administrators; and Dr. Blake Haselton, Executive Director, Kentucky Association of School Superintendents.

The members of 3KT want to thank Gov. Steve Beshear, the leadership of the General Assembly and the members of this task force for a variety of reasons. We appreciate the achievements to address public employee pension reform in the short-term during the special legislative session earlier this summer. On June 3, our partnership was among the very first to endorse that special session because we do understand the crisis we face in Kentucky.

We appreciate the commitment which you members of this task force have made by accepting months of study and deliberation to develop recommendations for long-term solutions. We know that you face complex questions and limited options, and pledge to be a resource to you in that work.

Your work is not merely one of significance to the thousands of men and women working in Kentucky's schools and universities, city, county and state government agencies. The changes that will culminate from your efforts will affect every taxpayer, every public service user, and most importantly in our view, every child in every public school in Kentucky for years to come.

As organizations of local school leaders, budget managers and personnel administrators, we have focused our attention on matters relating to the retirement programs of our invaluable classified employees. These are the nearly 50,000 people who transport our children to and from school, who provide the nutritional meals to sustain them through the day, who ensure that the classrooms, playgrounds and gymnasiums are clean and safe, and who assist our teachers in all phases of instruction. All too often, when citizens think of schools and learning, they give their attention strictly to our wonderful teachers. But without the work of these professionals in our classified ranks, the teaching and learning experience during our school day could not be successful.

(more)

Briefly, I would like to address three points which the members of our collective organizations believe to be vital for your consideration.

We encourage the task force to set among its goals:

1. To ensure protection of the hard earned retirement benefits for our schools' classified employees;
2. To confirm the fiscal solvency of the retirement pools as a result of any changes that you propose; and
3. To avoid any negative consequences for Kentucky's already financially-strapped public school systems which are responsible for making the employer contribution. This represents an important difference from the situation regarding the retirement contributions made by the state on behalf of teachers and state employees.

Critical to each of these issues is the completion of the actuarial study of the Kentucky Retirement System which is underway. Our organizations believe it is essential that this study provides answers to several key questions:

1. What are the total assets contributed by school districts and school classified workers to the County Employees Retirement System (CERS)?
2. What are the benefits for these school workers to remain in the CERS pool, and conversely, what would be the ramifications of any shift of these employees to a different retirement system or structure?
3. What is the projected fiscal impact to school districts of any ultimately-recommended changes in the state's public employee retirement systems?
4. What must be done to end the practice of diverting resources from the Kentucky Teachers' Retirement System's (KTRS) pension fund to the KTRS medical insurance fund, while ensuring that retired teachers continue to have access to quality health insurance? We understand that topic initially may not have been stated as part of your purview, but we believe it is an essential issue that cannot be overlooked.

I cannot overemphasize the fundamental necessity to your work that these four questions are answered with as much certainty as is possible. When this actuarial study is completed, we would welcome the opportunity to respond to those findings as you proceed toward your final recommendations.

Kentucky's public school leaders are grappling with challenges in concert with our counterparts who lead our cities, our counties and our state. We are being forced to divert needed resources from the classroom to fund these employee benefits. Many of our districts this new school year have reduced teachers and/or support staff as a direct consequence of the budget balancing realities.

The Kentucky School Boards Association is in the process of gathering district personnel data for the new school year. Of the 125 districts responding to the survey to date, 80 report having had to reduce staff by more than 883 positions. That represents a loss of more than 10 positions on average for each of the districts we have heard from so far.

For example, Perry County Superintendent John Paul Amis reports having to release 45 teacher aids who were working with struggling students in each of his district's 13 schools. This means less individual attention for all students in those classrooms.

In Somerset Independent, Superintendent Teresa Wallace told of the loss of 23 staff, including 16 elementary teachers. This will mean a significant increase in the teacher/student radio, raising the average class size from 20 to 22 up to 25 to 27.

In each case, the situation is compounded by reduced funding in such vital areas as student tutoring, professional development for teachers, alternative classroom programs, and school resource officers.

At the same time, Kentucky districts are delaying necessary facility, technology, transportation and other infrastructure improvements that we know to impact a quality learning atmosphere. While state funding for school transportation has been flat lined, we share the pain of every Kentucky family with the rising cost of bus fuel needed to bring our children to and from school and transport them to valuable learning opportunities through field trips and extracurricular activities.

In closing, we believe that, at a time when Kentucky's economic situation has forced the governor and the legislature to provide less school funding than we all know is necessary, our state cannot take any step that further erodes the financial resources devoted to classroom learning. Our teachers are challenged to provide world class instruction. Our students are being pressed to demonstrate higher levels of thinking. Our school and district leaders are expected to make both of those targets achievable, despite insufficient resources. Just as we cannot allow our public employee pension funds to continue on the path to insolvency, neither can we support any actions which threaten to reverse our commitment to a brighter future for our state through a better educated population.

Again, our organizations want to thank the members of this task force for the vital service that you are performing. We pledge to remain an active resource to you over the coming months.

# # #

July 22 working group on CERS
Talking points

Introductory Remarks:

- Kentucky League of Cities is a membership organization of 381 cities in Kentucky. Approximately 220 cities in Kentucky participate in the County Employee Retirement System.

- KLC and it's members have been calling for significant reform to the County Employee's retirement system for the last several years because of the escalating and unaffordable employer contribution rates cities must pay. .

- City officials recognize that our employees, both uniformed and non-uniformed, serve as the backbone to the services that our cities provide. Because of the unaffordable contribution rates, many cities have been forced to eliminate public safety positions, cut financial support to social service groups or tap rainy day funds in the face of skyrocketing pension and retiree health insurance costs.

- The Bottom line for Kentucky's cities is that we are in search of changes that will make employer contribution rates more affordable in the short term or we will continue to see cities making these difficult decisions and sacrifices that can have a negative impact on the quality of life of our citizens.

- While the reforms passed during the special session are an excellent start, we will remain diligent in our pursuit of a system that cities can afford now. We see the dialogue on this subcommittee as an important avenue to that end.

Special Session Impact

- HB 1 brought cities some important relief for cities and counties through:

    - Raising retirement ages and service requirements for future hires;
    - Lowering the annual pension cost of living adjustment to 1.5 percent; and
    - Requiring new employees to contribute 1 percent of their salary to the retirement health insurance fund
    - And, the immediate impact of temporarily reducing the employer contribution rate for the next fiscal year. These changes are projected to save CERS agencies over $50 million this fiscal year.

- These changes go a long way to addressing cities' retirement woes, but our cities recognize that once the one year rate reduction established by HB 1 ends, cities will likely once again see rapidly rising employer contribution rates established by the KRS unless more is done in the 2009 session to provide additional retirement cost reductions. Our cities are confident that this workgroup process can lead to recommendations that could create needed efficiencies in the retirement system.

Issues for the working group

- Since HB 1 addressed many of the long term changes that were needed, Our top priority in participating in the subcommittee and in the next session is to obtain lasting reductions in employer contribution rates that can immediately impact city budgets.

  - Governance: In the last regular session, our cities were attracted to the proposal to create a separate LGERS board to manage the retirement system for city and county employees. .In the view of our cities, this option would have created a board more responsive to the unique needs of city and county employers and would have permitted those most impacted to have more of a role in the decision making process. The evaluation of CERS currently being performed by the actuaries should shed additional light on the feasibility of this option. Regardless of the outcome, our cities desire additional representation on any retirement board tasked with making these far-reaching decisions. Another option may be to increase the number of CERS representatives on the KRS board of trustees and to require that those representatives have significant local government experience. Cities see the governance issue closely tied to the "money issue" and think that additional representation in the decision-making could have some impact on employer contribution rates.

  - Our cities believe the Kentucky Retirement Systems should use a less aggressive approach to pushing CERS toward full funding. Unlike the state, CERS employers have paid their retirement bills and should be allowed a 10 year phase-in to full funding. "Full funding" should be defined as 85% of full funding, a level many retirement actuaries deem adequate Defining a standard in statute could be a solution that gives trustees responsible for the administration of the retirement system comfort that less aggressive approaches will not violate fiduciary obligations. Clearly, addressing this issue could have an immediate impact on the employer contribution rates.

  - It's no secret that the health insurance coverage provided to retirees is the main cost-driver for local governments with employees in CERS. Fortunately, HB 1 provided that all employees hired after Sept. 1 contribute 1 percent of their salary toward their retirement insurance costs.

That is a welcome change for CERS employers because they have been paying the full cost of retirement health insurance , however additional efficiencies will be needed to reduce the burden of spiraling medical costs. KLC looks forward to participating on the health care subcommittee that is tasked with examining this issue and is optimistic that ideas will surface that have the potential of having an instant impact on city budgets.

- The new HB 1 restrictions on "double-dipping" , especially for hazardous duty employees, requires retirees who return to a hazardous duty position to pay for the health insurance portion of the benefit twice. Some of our small cities have raised concerns that this new requirement will make it more difficult to hire retired police officers for important public safety positions in their communities. We are anxious to discuss solutions for this barrier in the working group.

- Since questions have been raised about structural subsidies benefiting one or more of the groups in CERS we look forward to the results of the valuation study being conducted by the KRS actuary. This is the most thorough evaluation to date of CERS assets, liabilities and possible subsidies that benefit certain participants. We are hopeful that the actuarial recommendations will allow us to move forward in a manner that is fair to all agencies in CERS. Again, we think that there is a possibility that changes in this area could produce much needed short-term relief for local governments

Conclusion

- Thank the Governor for the opportunity to participate in the working group.
- Thank legislators for the solid first step of the special session.
- Recognize Auditor Luellen and Joe Meyer as chair and vice chair.
- KLC is committed to working with all of those that will be impacted by potential changes, and we realize that these are tough issues – but we do not think that cities can be complacent and continue to absorb drastic employer contribution rates in the near future and still be able to maintain or enhance the quality of life in our communities expected by our citizens.

KENTUCKY PUBLIC EMPLOYEES WORKING GROUP
CERS/LGERS Subcommittee
Testimony by the Kentucky Education Association
July 22, 2008

Good morning Chairman LuAllen and members of the study group. My name is Tom Denton, KEA Vice President. I'm speaking today on behalf of KEA President Sharron Oxendine, who is attending the NCSL Conference today. With me is Helen Cottongim, bus driver from Boone County who represents classified school employee members on the KEA Board of Directors. KEA appreciates the opportunity to offer our initial comments regarding these proposals as background to the study group.

Of KEA's approximately 40,000 members, almost 5,000 members are active and retired classified school employees. While we represent only about 10% of such employees, we are the only organization with a substantial number of classified members statewide. We are honored to speak for these hard-working school secretaries, bus drivers, custodians, and classroom aides, who are covered by the County Employee Retirement System.

KEA applauds Governor Beshear's inclusion, in his Executive Order, of a study committee to review proposals to change the current makeup of the County Employees Retirement System. The various proposals we have heard discussed include transferring classified school employees and retirees out of CERS to another retirement system, moving non-school members of the CERS into a newly created Local Government Employee Retirement System, or some combination.

All of these proposals appear complex and far reaching in their impact, not only on classified school employees, whom KEA represents, but all the current members of the CERS, as well as the retirement systems themselves. They raise important questions about how assets would be fairly divided and how such a massive movement of people and assets from one retirement system to another would be accomplished. They also raise the question of why such a change should be made.

For these reasons, KEA has not advocated moving classified school employees from CERS. Rather, we have strongly and consistently stated our belief that a thorough study is needed of these various proposals and their impacts before any action is taken.

We strongly support an actuarial study to examine the assumptions which underlie these proposals. That should help all the parties understand, for example, whether or not (or to what degree) one group may be subsidizing another. City and county employers appear to believe that they are subsidizing retiree health insurance costs for classified school employees. KEA believes that the state and members of the state health insurance group subsidize city and county employers because their active employees are not part of the state group until they retiree as "unescorted retirees." An actuarial study should examine and clarify these and other complex issues.

The issues under study will not only impact classified school employees; they also raise important policy issues that will impact all Kentuckians. Kentucky faces a critical shortage of bus drivers and is beginning to see a similar shortage in skilled trades and custodial workers. Resolving the issues under study in a way that maintains a well funded and secure pension benefit is critical to the recruitment and retention of qualified people to fill these crucial education positions.

Finally, I'd like to remind the committee that these decisions affect very real, hard-working Kentuckians. They are not just numbers on a page. They are your son's bus driver, the retired secretary who comforted your daughter when she went to the office with an upset stomach, the classroom aide who is helping your niece learn to read and the classroom aide who is helping your niece learn to read, and the lunchroom worker who makes sure your child has a hardy breakfast and nutritious lunch so that they will be ready to learn. These hard working people are critical to public education and the services they provide are essential to student learning.

Yet, when these critically import people retire they draw exceptionally small pensions; most get well below $10,000 annually. Even with Social Security, many live below the poverty level throughout their old age. They are understandably very concerned about how changes to their retirement system will impact them.

KEA looks forward to engaging on these important issues. We stand ready to bring forward additional testimony in the future as this process unfolds and more detailed information becomes available.

Thank you.

Kentucky Teachers' Retirement System

Gary L. Harbin, CPA
Executive Secretary

CERS Overview

Information for

Kentucky Public Pension Working Group

August 18, 2008

AGENDA

- Recap CERS information
- Discuss process if transferred to KTRS

CERS Overview

Kentucky Public Pension Working Group
CERS/LGERS Subcommittee

Mike Burnside
Executive Director, KRS

CERS Non-Hazardous Composition as of July 15, 2008*

	Classified School Board Employees	City and County Employees	Total
Active Members	48,863	36,415	85,278
Inactive Members			
Vested	4,961	3,656	8,617
Non-vested	30,129	18,394	48,523
Retirees/Beneficiaries	20,217	17,453	37,670
Total	**104,170**	**75,918**	**180,088**

*** Numbers only reflect the current or last known participating employer.**

An active city or county employee could also be counted as an inactive school board employee and vice versa. Computer database unable to make that distinction

CERS Demographics in 2001

- City and county employees
  - 42% of total membership
  - 59% of gross reported salary
- Classified school board employees
  - 58% of membership
  - 41% of gross reported salary
  - Full year credit for 10 months (180 days) of service

Mercer Analysis 9/25/02

- Assumed demographics of city and county employees *identical* to classified school board employees
  - Average age, mortality rate, turnover ratios, claims experience, etc
- For fiscal year 2001, cities and counties would have saved 1.49% ($13.8 million) if rated separately
  - Based solely on a ratio of expenses to members

Next Steps

- Full actuarial analysis, starting with an experience study to establish appropriate assumptions that will allow an accurate determination of the amount of any subsidy
  - Original study by Mercer assumed no demographic differences
  - Ohio and Missouri systems indicate there may be significant demographic differences

Tom Cavanaugh

CEO, Cavanaugh Macdonald Consulting, LLC

CERS Reorganization Study

- Determine proper actuarial assumptions
- Perform pension and insurance valuations for each group (School Board and City/County)
- Measure the subsidy, if any
- If a material subsidy exists, split assets

Actuarial Assumptions

- Anecdotal evidence suggests that at least the termination, retirement and mortality rates differ between the two groups
- Other state experience with separate retirement systems for School Board employees supports this (GA, MO, OH)
- Conduct experience investigation of the two groups to substitute facts for impressions

Actuarial Valuations

- Run valuations for both pension and health care separately for the two groups
- Use both current assumptions and those developed in the experience investigation
- Compare employer normal cost contribution rates to determine the amount and direction of any subsidy

Asset Split

- Assuming a material subsidy exists, the current assets would be split between the two groups
- Use the actuarial accrued liability of the two groups as measured by the experience investigation assumption set
- Cover retiree liability and accumulated active member contributions at 100%
- Split the remaining assets by the ratio of active member accrued liability

Long-term Impact

- Run 20 year projections of the two groups separately after the split has occurred
- It would appear the only viable option for the future is to continue separate valuations for the School Board members with independently determined employer contribution rates

Options for Placement

- Potential new home for School Board members:
  - KERS
  - KTRS
  - Stand-alone School Board Retirement System
  - CERS
- Given that School Board members will be valued separately after the split, the most efficient choice is CERS

Operational Considerations

- Governance
  - School Board employees may need representation on the governing board
  - Statutory and regulatory changes will be necessary
- Administration
  - Classified employee benefit structure different from KERS, SPRS or KTRS—where do they go?
  - Transfer to KTRS?
    - KTRS would have to develop a new system to accommodate classified employees
    - KTRS hire and train staff, or downsize KRS if it loses 104,000 members?
    - Physical transfer of member records from KRS to KTRS
  - Status of inactive members? Retired members?

Operational Considerations

- Administration (con't)
  - Transferring employee credit
    - Many employees have credit in more than one system/agency and may require a manual records search
    - Must identify proper amount of service credit to be transferred with employee record
    - Employees with credit in more than one system may receive multiple retirement checks—one from each system
    - Computerized records only go back to 1996--Difficulty identifying actual employee and employer contributions

Operational Considerations

- Administration (con't)
  - Asset transfer must comply with all IRS/SEC restrictions
  - Asset transfer must be done over a number of months/years for protection against market fluctuations
  - Restructured investment trusts will require new asset liability model for investments
  - Extensive effort to rebalance accounts to stay within the allowable asset allocation ranges

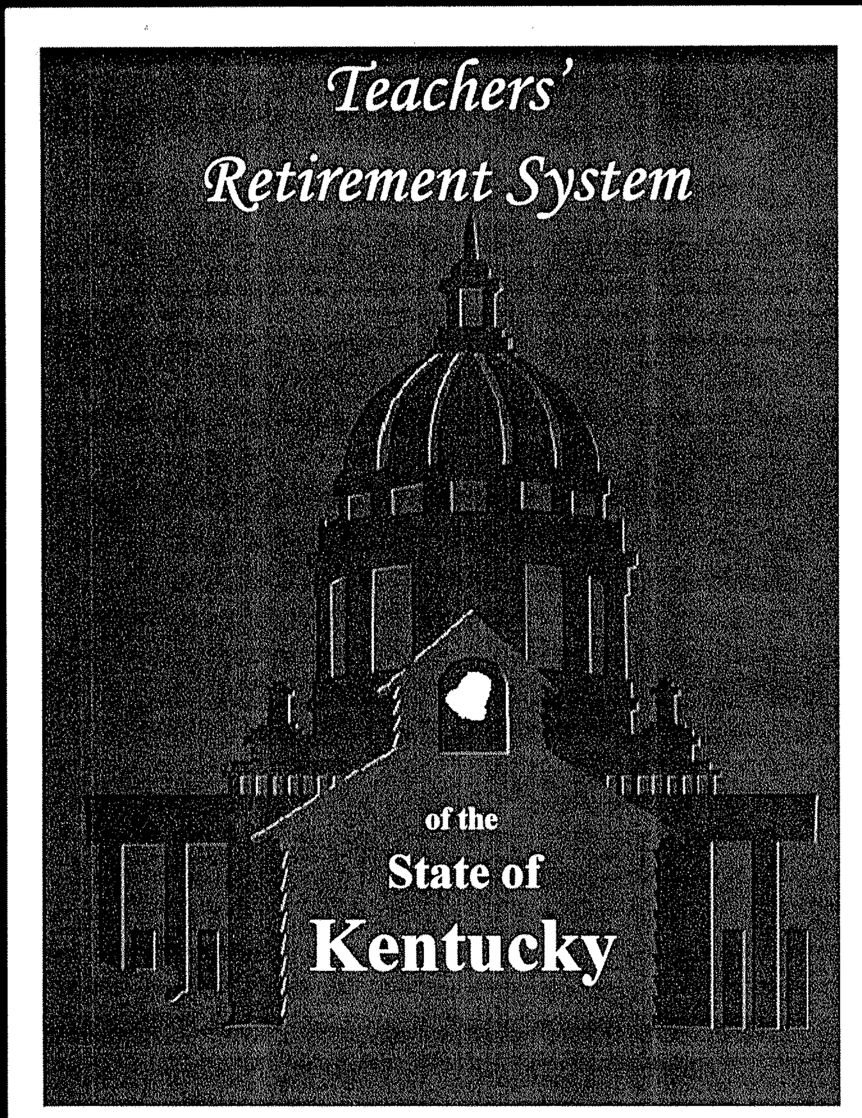
Discuss Aspects of Transferring Classified School Board Employees to KTRS

Overview

- The differing benefit structure will require a separate system under KTRS.

Timing of Transfer

- Approximately 18-24 months
- Facility Needs
- Computer Systems
- Staffing
- Valuation & Transfer of Assets
- IRS Approvals



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CERS Overview

Kentucky Public Pension Working Group
CERS/LGERS Subcommittee

Mike Burnside
Executive Director, KRS

CERS Overview

- Statistical overview of CERS
- Historical perspective of CERS/LGERS issue
- What are the next steps?
- Operational considerations

Statistical Overview

- CERS was established by statute in 1958
  - Optional system for City and County employees
- 1964 – Local school boards began joining
- 1974 – All school boards required to join by July 1, 1976
- 1988 – all cities with existing defined benefit plans must join by August 1, 1988
  - Thereafter, any city establishing a DB plan could only do so in CERS

CERS Non-Hazardous Composition as of July 15, 2008*

	Classified School Board Employees	City and County Employees	Total
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CERS Funding Ratios as of June 30, 2007

(% of Actuarial Assets to Actuarial Liabilities)

	2002	2003	2004	2005	2006	2007
Pension Fund	129.6	119.7	105.1	94.0	83.6	82.1
Insurance Fund	22.8	23.9	24.0	23.8	16.9	28.8

Health Care for Retirees

- KRS pays for health care for all retirees
  - Hired prior to July 1, 2003 – pay full single premium
    - Under age 65 – insured under Kentucky Public Employee Health Insurance Plan
    - Over age 65 – Medicare supplement through KRS
  - Hired on/after July 1, 2003
    - $10/month/year of service, adjusted for COLA
    - Applied toward premium in employee health plan or Medicare supplement

Increasing Health Care Costs

- Growth in the Unfunded Actuarial Liability
- Increase in the EMPLOYERS' Annual Required Contribution for pension benefits
- Increase in the state health plan premiums for both employers and employees

Historical Perspective

- October 2001 – Group Health Insurance Board (GHIB) Annual Report
  - Local Government Unescorted Retirees
    - Under age 65
    - Local government employers generally do not insure active employees through the Public Employee Health Insurance group plan
    - Added $10 million to total cost in fiscal year 2000
- GHIB continued to update cost amount in annual reports through 2004
  - $21 million in 2003

Personnel Cabinet Initiative - 2002

- Requested relief from unescorted retirees
  - Require all agencies with non-Medicare eligible retirees to participate in the group plan for active employees; or
  - Require agencies with unescorted retirees to pay Personnel for the actuarial cost difference of their non-Medicare eligible retirees

2002 Regular Session

- HB 846
  - Filed on March 4, 2002
  - Required separate rating for unescorted retirees
  - Non-participating agencies required to pay subsidy for each unescorted retiree
  - Amended to require study by Interim Joint Committee on State Government by Nov 1, 2003
    - LRC retained Segal for actuarial analysis
    - Oct 2002 - Segal reported added costs of $14.1 million from unescorted retirees in 2001

2002 KRS Actuarial Study for CERS Employers

- KRS actuary, Mercer Human Resources Consulting
  - Determine the amount of subsidy that city and county employers pay for school board employees through their ARC to CERS

CERS Demographics in 2001

- City and county employees
  - 42% of total membership
  - 59% of gross reported salary
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  - Average age, mortality rate, turnover ratios, claims experience, etc
- For fiscal year 2001, cities and counties would have saved 1.49% ($13.8 million) if rated separately
  - Based solely on a ratio of expenses to members

2003 Regular Session

- HB 103
  - Cities and counties would pay actuarial amount of additional cost for unescorted retirees
  - KLC and KACO agreed to pay, provided the bill also addressed the "subsidy" they were paying for classified school board employees in CERS
  - HFA 1 required Dept of Education to request general fund support to cover classified school board employees in CERS
  - Bill was never passed by the House

Subsequent Actions

- June 25, 2003 – Interim Joint Committee on State Government
  - KEA, KLC and KACO agreed to the compromise language in HB 103
- HB 11 filed in 2004 Regular Session
  - Included compromise language of HB 103
  - State would provide funding for classified school board employees in CERS
  - Passed House 94-0
  - Bill stalled in Senate and was not passed

Subsequent Actions

- 2005 – KRS updated the Mercer study
  - Using same assumption – no demographic differences
  - Projected that cities and counties would spend $23.8 million less in 2007-2008 if they were rated separately
- No legislative action taken from 2004 until 2008 Regular Session

2008 Regular Session

- HB 600 SCS
  - Established LGERS for cities and counties
  - Separate board of trustees for LGERS
  - Placed classified school board employees in KERS
  - Silent on the issue of unescorted retirees in the KY Public Employee Health Insurance plan
  - Inadequate time to conduct a full actuarial analysis
  - No pension bill passed during Regular Session
- CERS/LGERS language omitted in special session

Next Steps

- Full actuarial analysis, starting with an experience study to establish appropriate assumptions that will allow an accurate determination of the amount of any subsidy
  - Original study by Mercer assumed no demographic differences
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Tom Cavanaugh

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- Assuming a material subsidy exists, the current assets would be split between the two groups
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Long-term Impact

- Run 20 year projections of the two groups separately after the split has occurred
- It would appear the only viable option for the future is to continue separate valuations for the School Board members with independently determined employer contribution rates

Options for Placement

- Potential new home for School Board members:
  - KERS
  - KTRS
  - Stand-alone School Board Retirement System
  - CERS
- Given that School Board members will be valued separately after the split, the most efficient choice is CERS

Service Credit Issue

- Asset split will be based on the reported CERS service of the School Board and City/County active members
- If School Board members are moved to a new system, all CERS service should move with them, and all City/County members should retain all CERS service credit

Operational Considerations

- Governance
  - School Board employees may need representation on the governing board
  - Statutory and regulatory changes will be necessary
- Administration
  - Classified employee benefit structure different from KERS, SPRS or KTRS—where do they go?
  - Transfer to KTRS?
    - KTRS would have to develop a new system to accommodate classified employees
    - KTRS hire and train staff, or downsize KRS if it loses 104,000 members?
    - Physical transfer of member records from KRS to KTRS
  - Status of inactive members? Retired members?

Operational Considerations

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  - Transferring employee credit
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  - Extensive effort to rebalance accounts to stay within the allowable asset allocation ranges

Questions?

Kentucky CERS Working Group

Subsidy Study Results

September 25, 2008

Basic Retirement Funding Equation

$$\mathbf{C + I = B + E}$$

C = Contributions
I = Investment Income
B = Benefits Paid
E = Expenses (administration)

Basic Retirement Funding Equation

$$C + I = B + E$$

B depends on

- Plan Provisions
- Experience

C depends on

- Short Term: Actuarial Assumptions
  Actuarial Cost Method
- Long Term: I, B, E

CERS Reorganization Study

- Determine proper actuarial assumptions
- Perform pension and insurance valuations for each group (School Board and City/County)
- Measure the subsidy, if any
- If a material subsidy exists, split assets
- Measure long term impact of a split

Actuarial Assumption Types

- Decremental
- Economic

Decremental

- Withdrawal
- Death while active
- Disability
- Retirement
- Death after retirement

Economic

- Inflation
- Real return for assets
- Salary increases
- COLA's

Group Demographics

Item	School Board Members	Non-School Board Members
Actives		
Number	48,646	36,274
Average Age	47.1	44.2
Average Service	8.0	8.2
Average Annual Salary	$17,592	$33,662
Retirees		
Number	18,907	16,657
Average Annual Benefit	$6,531	$14,052
Inactives		
Number	31,370	22,531

Actuarial Assumptions

- Conducted experience investigation of the two groups to substitute facts for impressions
- Results reported in 9/5/08 letter.
- Changes made in the termination, retirement and mortality rates for both groups. All other assumptions were as currently used for valuation purposes.

Actuarial Valuations

- Run valuations for both pension and health care separately for the two groups
- Use both current assumptions and those developed in the experience investigation
- Compare employer normal cost contribution rates to determine the amount and direction of any subsidy

Asset Split

- Assuming a material subsidy exists, the current assets need to be split between the two groups
- Use the actuarial accrued liability of the two groups as measured by the experience investigation assumption set
- Cover retiree liability and accumulated active member contributions at 100%
- Split the remaining assets by the ratio of active member employer-financed accrued liability

Results of Subsidy Calculations

		School Board	Non-School Board	School Board	Non-School Board
Item	**June 30, 2007 Valuation Results**	**Current Assumptions**		**New Assumptions**	
		Pension			
Normal Cost Rate*	4.53%	4.71%	4.40%	1.93%	2.36%
UAL Rate	3.23**	2.24	2.33	1.74	1.80
Total Rate	7.76%	6.95%	6.73%	3.67%	4.16%
Assets at Market Value	$5,812,935,251	$2,112,520,139	$3,700,415,112	$2,116,027,006	$3,696,908,245
		Insurance			
Normal Cost Rate*	6.32%	8.82%	4.56%	6.72%	3.84%
UAL Rate	6.43**	8.37	4.50	8.38	4.55
Total Rate	12.75%	17.19%	9.06%	15.10%	8.39%
Assets at Market Value	$1,084,042,781	$522,294,284	$561,748,497	$518,819,701	$565,223,080

* includes expenses of .59% for pension and .15% for insurance.
** based on actuarial value of assets.

Impact on Employer Contributions – FY 2009

	School Board			Non-School Board	
Combined	Current Assumptions	New Assumptions	Combined	Current Assumptions	New Assumptions
			Pension		
$62,799,826	$63,993,415	$33,792,206	$90,081,694	$88,888,106	$54,944,208
			Insurance		
$114,171,586	$158,280,115	$139,036,052	$163,770,675	$119,662,145	$110,812,958
			Total		
$176,971,412	$222,273,530	$172,828,259	$253,852,369	$208,550,251	$165,757,166
			Level of Subsidy		
	$45,302,118			$(45,302,118)	

Long-term Impact

- Run 20 year projections of the two groups separately after the split has occurred
- It would appear the only viable option for the future would be to continue separate valuations for the School Board members with independently determined employer contribution rates

Projection Results

		School Board			Non-School Board	
Fiscal Year Ending June 30	Pension	Insurance*	Total	Pension	Insurance*	Total
2009	3.67%	15.10%	18.77%	4.16%	8.39%	12.55%
2012	3.95	14.02	17.97	4.50	7.24	11.74
2016	4.96	13.10	18.06	5.59	6.37	11.96
2020	6.38	12.55	18.93	7.09	5.83	12.92
2024	8.30	12.52	20.82	9.09	5.55	14.64
2028	10.83	12.78	23.61	11.77	5.46	17.23

* Takes into account the 1% employee contribution under HB 1 for new hires.

Options for Placement

- Potential new home for School Board members:
  - KERS
  - KTRS
  - Stand-alone School Board Retirement System
  - CERS
- Given that School Board members will be valued separately after the split, the most efficient choice is CERS

Service Credit Issue

- Asset split will be based on the reported CERS service of the School Board and City/County active members
- If School Board members are moved to a new system, all CERS service should move with them, and all City/County members should retain all CERS service credit

Summary

- A subsidy exists between School Board and Non-School Board Employers in CERS.
- If a split is legislated, both groups should remain in CERS.
- Actual asset split will be determined based on a valuation of the two groups as of the effective date of the split.

Appendix III

Actuarial Analysis of Potential CERS Split

Cavanaugh Macdonald Consultants

Cavanaugh Macdonald
CONSULTING, LLC
The experience and dedication you deserve

October 9, 2008

Mr. William A. Thielen
Chief Operations Officer
Kentucky Retirement Systems
Perimeter Park West
1260 Louisville Road
Frankfort, KY 40601

Subject: Actuarial Analysis of Potential CERS Split – FY 2008 Subsidy

Dear Bill:

As requested, we have analyzed the impact on CERS if the membership were split between School Board employees (SB) and all other employees (NSB). The results of our analysis, which includes a comparison of employer normal cost contribution rates and a twenty year projection of results, are presented below.

Potential CERS Split

We were requested to perform a study to determine if any subsidy existed between the SB and NSB employers covered under CERS. The impression was that there is some subsidy due mainly to the difference in demographics, particularly salaries between the two groups. The table that follows shows some of the pertinent information.

The direction and size of any subsidy was to be determined by comparing the normal and total contribution rates for the two groups separately. If a material subsidy did exist, assets were to be split between the two groups and 20 year projections performed to analyze the impact of splitting the groups for future contribution rate calculations.

3550 Busbee Pkwy, Suite 250, Kennesaw, GA 30144
Phone (678) 388-1700 • Fax (678) 388-1730
www.CavMacConsulting.com

CERS Member Demographics

Item	School Board Members	Non-School Board Members
Actives		
Number	48,646	36,274
Average Age	47.1	44.2
Average Service	8.0	8.2
Average Annual Salary	$17,592	$33,662
Retirees		
Number	18,907	16,657
Average Annual Benefit	$6,531	$14,052
Inactives		
Number	31,370	22,531

Parameters and Assumptions

The first step in the study was to review the actual experience of the two groups so as to establish assumptions for use in the study that reflected the anticipated behavior of the SB and NSB members. That step in the study was completed earlier and reported to you in our letter of September 4, 2008. Results were then developed using both the current actuarial assumptions used for valuation purposes and the new set of assumptions.

The cost analyses were performed using the June 30, 2007 valuation results as a base, and comparing the employer normal and total cost contribution rates for each of the groups based on the current benefit structure for both pensions and health care. The market value of assets as of June 30, 2007 was split between SB and NSB by covering 100% of the retiree liability and active member accumulated contributions and then splitting any remaining assets by the ratio of the employer-financed active member accrued liability of the two groups. For health care, the existing assets were not sufficient to fully finance the retiree liability and so were split based on that liability alone.

In order to demonstrate the impact of the split on employers, twenty-year projections were done for both the pension and insurance funds. The projections were performed using the June 30, 2007 valuation results as a base, and projecting active and retired SB and NSB memberships for each of the funds over the twenty year period assuming the active population remained constant in number. We then performed valuations of the populations annually to develop the contribution rates. In developing the projection results, the impact of the benefit changes made by HB 1 were fully reflected for new hires.

Results

The table below shows, for each of the funds, the employer contribution rates assuming for the unfunded accrued liability (UAL) portion of the rates that assets were split as described above. The resulting asset values are also shown. For comparison purposes, the actual June 30, 2007 valuation results are also shown. **It must be noted that the actual valuation results are based on the smoothed actuarial value of assets which were lower than the market value on June 30, 2007.**

As can be seen, there is a small subsidy under the pension fund in favor of the SB employers on the new assumptions, and a material subsidy under the insurance fund in favor of the NSB employers under both assumption sets. This result is not unexpected. The pension benefits are directly related to salary, and the different demographics and experience of the groups would suggest that the employer rates would be relatively equal as a percent of pay, but slightly lower for SB employers. Similarly, given the fact that the health care benefit levels are approximately the same for all members, it would be expected that the SB employers would exhibit a higher contribution rate than NSB employers to finance this benefit as a percent of pay given the much lower average pay of SB members.

Results as of June 30, 2007

Item	June 30, 2007 Valuation Results	School Board	Non-School Board	School Board	Non-School Board
		Current Assumptions		New Assumptions	
Pension					
Normal Cost Rate*	4.53%	4.71%	4.40%	1.93%	2.36%
UAL Rate	3.23**	2.24	2.33	1.74	1.80
Total Rate	7.76%	6.95%	6.73%	3.67%	4.16%
Assets at Market Value	$5,812,935,251	$2,112,520,139	$3,700,415,112	$2,116,027,006	$3,696,908,245
Insurance					
Normal Cost Rate*	6.32%	8.82%	4.56%	6.72%	3.84%
UAL Rate	6.43**	8.37	4.50	8.38	4.55
Total Rate	12.75%	17.19%	9.06%	15.10%	8.39%
Assets at Market Value	$1,084,042,781	$522,294,284	$561,748,497	$518,819,701	$565,223,080

* includes expenses of .59% for pension and .15% for insurance.
** based on actuarial value of assets.

The next table compares the contribution amounts based on the two assumption sets, actual FY 2008 payrolls and **market value of assets**. Also shown are the "Combined" contributions which are the total contributions for both groups under current assumptions allocated based on payroll alone. Comparing the "Combined" figures with the "Current Assumptions" figures provides a measure of the dollar subsidy in FY 2008, which is shown at the bottom of the table as $43,775,319. Comparing "Current Assumptions" figures to "New Assumptions" figures provides an indication of the direction the actual contributions will move if the split is legislated. The reduction in these latter numbers is different for the two groups because of the impact of the different assumptions used for each.

FY 2008 Employer Contributions

	School Board			Non-School Board	
Combined	Current Assumptions	New Assumptions	Combined	Current Assumptions	New Assumptions
		Pension			
$60,909,980	$62,063,342	$32,773,017	$86,598,070	$85,444,708	$52,815,748
		Insurance			
$110,884,352	$153,506,309	$134,842,657	$157,648,563	$115,026,605	$106,520,223
		Total			
$171,794,332	$215,569,651	$167,615,673	$244,246,632	$,200,471,313	$159,335,971
		Level of Subsidy			
	$43,775,319			$(43,775,319)	

Since the subsidy level as a percentage of payroll is not very different between current and new assumptions, the projection results below are shown using the new assumptions. A similar pattern would result using the current assumption set.

CERS Split Employer Contribution Rates

Fiscal Year Ending June 30	School Board			Non-School Board		
	Pension	Insurance*	Total	Pension	Insurance*	Total
2009	3.67%	15.10%	18.77%	4.16%	8.39%	12.55%
2010	3.61	14.40	18.01	4.13	7.92	12.05
2011	3.77	14.20	17.97	4.29	7.56	11.85
2012	3.95	14.02	17.97	4.50	7.24	11.74
2013	4.17	13.84	18.01	4.73	6.97	11.70
2014	4.41	13.61	18.02	5.00	6.74	11.74
2015	4.67	13.34	18.01	5.28	6.54	11.82
2016	4.96	13.10	18.06	5.59	6.37	11.96
2017	5.27	12.90	18.17	5.92	6.21	12.13
2018	5.60	12.74	18.34	6.29	6.06	12.35
2019	5.98	12.63	18.61	6.68	5.93	12.61
2020	6.38	12.55	18.93	7.09	5.83	12.92
2021	6.81	12.51	19.32	7.54	5.74	13.28
2022	7.27	12.49	19.76	8.02	5.66	13.68
2023	7.77	12.50	20.27	8.54	5.60	14.14
2024	8.30	12.52	20.82	9.09	5.55	14.64
2025	8.88	12.56	21.44	9.68	5.51	15.19
2026	9.49	12.62	22.11	10.32	5.48	15.80
2027	10.13	12.70	22.83	11.01	5.47	16.48
2028	10.83	12.78	23.61	11.77	5.46	17.23

* Takes into account the 1% employee contribution under HB 1 for new hires.

In total, the subsidy remains fairly constant over the 20 year period. The difference in employer contribution rates (taking into account the 1% additional contribution to health care for new hires) is approximately 6.25% of payroll.

Comments

The following comments must be kept in mind when reviewing the results presented in this letter:

- The asset split is based on data available as of June 30, 2007. A complete audit of active, inactive and retired member service will be necessary if a split is legislated. That audit will likely take many months. A final asset split can only be determined once that is complete, so an adjustment in assets and therefore employer contributions will have to be made at some point in the future.

- The new assumption set used for purposes of determining the level of any subsidy resulted in lower contribution rates than the current assumptions used for valuation purposes generate. It is not recommended that any changes be made at this time in the valuation assumptions unless the split actually occurs. If the split is not legislated the experience of CERS members will be measured at the next regularly scheduled investigation and changes necessary will be recommended to the Board of Trustees at that time.

- If a split is legislated, the actual asset allocation will be determined by valuations of the two groups as of the effective date of the split. Given the likely changes in asset values and demographics, the actual asset allocation is likely to be different than that shown above, which will impact the level of subsidy. In particular, it is possible the market value of assets will be below the actuarial value at the time of any split. If that is the case, the split could possibly result in a short term increase in employer contributions for both groups. However, a material subsidy is still likely to exist.

If you need any further information regarding this analysis, please do not hesitate to contact us. The undersigned is a member of the American Academy of Actuaries and meets the Qualification Standards of the American Academy of Actuaries to render the actuarial opinion contained herein.

Sincerely,

Thomas J. Cavanaugh

Thomas J. Cavanaugh FSA, FCA, MAAA, EA
Chief Executive Officer

Copy to: R. Burnside

S:\Kentucky Retirement Systems\2008\Miscellaneous Correspondence\Actuarial Analysis CERS Split - Revised Subsidy doc

REVISED ESTIMATE

Here are the revised numbers.

Mike Burnside
Executive Director
Kentucky Retirement Systems
502-696-8800
Fax 502-696-8801

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From: Tom Cavanaugh [mailto:TomC@cavmacconsulting.com]
Sent: Thursday, October 09, 2008 8:48 AM
To: Thielen, Bill (KRS)
Cc: Burnside, Mike (KRS); Todd Green
Subject: RE: CERS Non-Hazardous WAGES for 2007-2008

Bill - Using current assumptions and the payroll below, the subsidy is $43,775,319. Using new assumptions and the payroll below, the subsidy is $32,608,681.

Tom

From: Thielen, Bill (KRS) [mailto:bill.thielen@kyret.com]
Sent: Wednesday, October 08, 2008 9:13 AM
To: Tom Cavanaugh
Cc: Burnside, Mike (KRS)
Subject: FW: CERS Non-Hazardous WAGES for 2007-2008

Tom,

See below for the 2007-2008 CERS Non-Hazardous employer wages.

William A. Thielen

Chief Operations Officer

Kentucky Retirement Systems

Tel: (502) 696-8444

Fax: (502) 696-8801

bill.thielen@kyret.com

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From: Mangum, Karen (KRS)
Sent: Wednesday, October 08, 2008 8:52 AM
To: Thielen, Bill (KRS)
Cc: Gibbs, Pam (KRS)
Subject: CERS Non-Hazardous WAGES for 2007-2008

TOTAL CERS Non-Hazardous WAGES:	2,162,607,058.45
CERS SCHOOL BOARD WAGES:	892,997,726.97
CERS NON-SCHOOL BOARD WAGES:	1,269,609,331.48

Let me know if you have any questions about the totals.

Thanks,

Karen Mangum

Information Technology
Kentucky Retirement Systems
karen.mangum@kyret.com
Phone: (502) 696-8617
or (800) 928-4646 ext. 8617

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Appendix IV

The Impact of "Unescorted Retirees"
An Actuarial Analsyis

PricewaterhouseCoopers

COMMONWEALTH OF KENTUCKY
KENTUCKY EMPLOYEES HEALTH PLAN

THE IMPACT OF "UNESCORTED RETIREES"
AN ACTUARIAL ANALYSIS

October 17, 2008

PRICEWATERHOUSECOOPERS

Contents

EXECUTIVE SUMMARY

This report provides an actuarial analysis of the impact on the Commonwealth of Kentucky's Kentucky Employees Health Plan of providing health coverage to non-Medicare eligible retirees from agencies that have chosen not to cover active employees under the same program.

The Personnel Cabinet of the Commonwealth of Kentucky has requested that PricewaterhouseCoopers (PwC) actuarially analyze the financial impact of the non-Medicare eligible retirees associated with agencies that do not have active employees ("unescorted retirees") participating in the Kentucky Employees Health Plan (KEHP) compared to specified active employee groups and non-Medicare eligible retirees associated with agencies that do have active employees participating in the KEHP program ("escorted retirees"). This report presents the results of this study. Where applicable this report compares results for the FY2008 period against the CY2006 and CY2007 periods.

This analysis evaluates the average cost difference between the unescorted retirees versus the specified actives, and the unescorted retirees versus the escorted retirees.

Key observations:

- There are currently at least two definitions being used to describe unescorted retirees. The KTRS definition is a more complex definition of the unescorted retirees. This study has maintained the technical definition of unescorted retirees as provided in the prior report, dated May 2, 2006: *Those covered retirees that come from an agency that does not cover its active employees in the state program.* It should be noted that the application of the technical definition to the available claims and enrollment data is complicated.
- The available enrollment and claims data do permit the separation of escorted and unescorted retiree groups from one another per a practical version of the above technical definition (discussed later in this report).
- On a per member per month basis, unescorted retirees cost approximately 64% more than the active members included in this analysis, and approximately 46% more than the blended costs of active members plus escorted retirees. These results are slightly less than those reported in 2006.
- Based on incurred claims data for the period July 2007 through June 2008, as compiled through the Thomson Reuters data warehouse, the total subsidized amount for unescorted retirees (for fiscal year 2008) was estimated to be approximately $37 million, or approximately $173 per unescorted retiree member per month.

Background

The Commonwealth of Kentucky, through its KEHP program, provides health care benefits to participating state and local government entities' non-Medicare eligible retirees and their dependents. Some of these government entities do not include their active employees in the KEHP plans (including many cities, counties, school boards, state universities, and local agencies), and instead independently provide coverage for these active employees. These same entities provide coverage for their non-Medicare-eligible retirees and their dependents through the KEHP program. This group of covered retirees is referred to as "unescorted retirees".

Under the KEHP program, active and non-Medicare eligible retired employees in the same plan option are assigned the same premium rate. This creates a situation in which, to some extent, the actives are subsidizing the non-Medicare eligible retiree costs. Retired non-Medicare-eligible employees' health care costs, on average, are higher than those associated with active employees. This cost difference can be significant. In the past the Personnel Cabinet has recommended various strategies to address the reduction or elimination of the subsidy.

The Kentucky League of Cities (KLC) has identified those active employee agencies that have the ability to reasonably pursue coverage other than through the KEHP program, and has requested that these agencies be excluded from this study for purposes of developing the active employee cost analysis. These agencies have been designated as "excluded" active agencies based on the agency listing provided by the Kentucky Retirement System (KRS) to KLC.

> For this analysis, PwC has not altered the KLC designation of excluded agencies and has based this analysis solely on the KLC designations. Furthermore, the list of excluded agencies provided by KLC reflects a KRS-maintained agency coding scheme that differs from the agency coding scheme available to PwC in the KEHP data. As a result, reasonable attempts have been made to manually match the excluded agencies by name (rather than code) per KLC against the agency names provided by KEHP and its third party data warehouse vendor, Thomson Reuters. This matching exercise is not precise. It is recommended that the attached listing of all agencies with the associated matched designations by active employee agency of "Included" or "Excluded" be provided to KLC for their review, comment, and approval.

This study estimates the degree to which active employees of non-excluded agencies are subsidizing the covered unescorted retirees based on the available enrollment and claims data.

> Throughout the remainder of this report, unless otherwise noted, references to "active employees" represents active employees of those agencies not designated as "excluded" by KLC.

DEFINITIONS

Key terms referenced in this report are.

Active Employees	Each covered individual currently employed by a participating Agency of the Commonwealth of Kentucky.
Active Employees (Included)	Those active employees associated with Agencies not identified by KLC per the "Active Employees (Excluded)" definition below.
Active Employees (Excluded)	Those active employees currently covered under the KEHP program who are associated with Agencies identified by KLC as having the ability to reasonably pursue coverage other than through the KEHP program.
Claims Completion	Related to incurred but not reported (IBNR) claims, claims completion represents the estimated percentage of claims in a given month that have already been reported. For example, a 95% completion factor means that the 95% of all claims incurred in a given month are actuarially estimated to have already been reported, with 5% remaining to be reported.
Contract	Coverage provided to a household, inclusive of all covered members in the household. "Per Contract Per Month" is synonymous with "Per Employee Per Month".
Credibility	In actuarial terms credibility refers to the extent to which it is felt that there is sufficient critical mass in the claims data so that valid conclusions can be drawn for projection and estimating purposes.
Escorted Retirees	Non-Medicare eligible retired employees (and their dependents) from agencies that provide coverage for their active employees through the KEHP program.
IBNR Claims	Also referred to as "incurred but not reported" claims. IBNR claims represent an actuarial estimate of claims that already have been incurred, but have not yet been submitted for payment to the insurance company or third party administrator.
Member	Each covered individual, whether he/she is an employee, non-Medicare eligible retiree, or dependent.

Per Employee Per Month	Also referred to as "PEPM". This is a measure of total monthly costs expressed on a per employee (or retiree) basis. Related dependent claims are associated with the named employee or retiree.
Per Member Per Month	Also referred to as "PMPM". This is a measure of monthly costs expressed on a per person basis, regardless of whether the person is an employee, retiree, or dependent.
Unescorted Retirees	Non-Medicare eligible retired employees (and their dependents) from agencies that do not provide coverage for their active employees through the KEHP program.

STUDY LIMITATIONS

Claims and Census Data Identification

This actuarial analysis of the financial impact of unescorted retirees on the KEHP program is based on the evaluation of claims experience for three distinct groups:

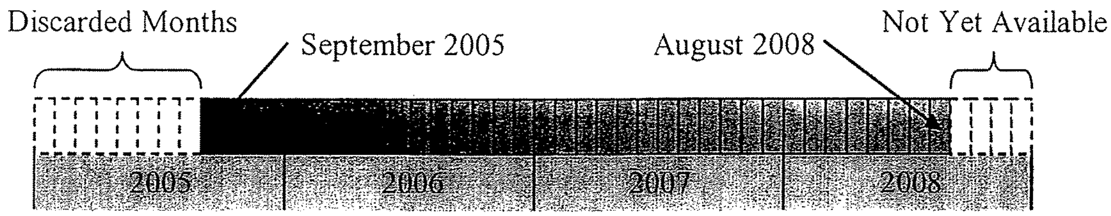
- Active employees and their dependents
- Escorted retirees, and their dependents
- Unescorted retirees and their dependents

The development of average experienced-based claims costs depends on the ability to identify the participating members in each of the above three groups.

Current and historic claims and eligibility data are provided by the Commonwealth's third party claims data warehouse vendor, Thomson Reuters, via its MedStat database. This database maintains historic claims and eligibility data on a rolling thirty-six month basis (*illustration 1*):

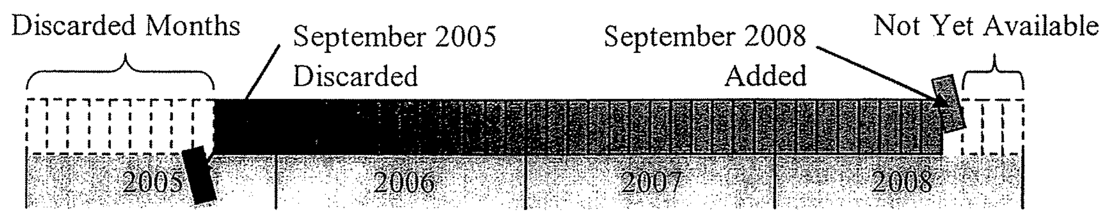
- As of the date of this report, the most recent month for which data are available is August 2008.
- Therefore, the earliest information in the database relates to claims and eligibility experience from September 2005.

Illustration 1



Once September 2008 data is available in the database, the September 2005 data will be "dropped off" of the available history, and the thirty-six months of rolling historic data will commence with October 2005 data (*illustration 2*).

Illustration 2



Once the September 2008 data are added, any claims and eligibility data contained in the September 2005 period would no longer be available. And, any information in that month on the associated agency for an active employee who had since retired would also be lost.

The available rolling 36 months of claims data identifies individuals as either active or retired in each month of the 36 month data period. If an individual retired prior to the 36 month time frame, there is no identification of the agency from which the individual retired in the file. Therefore, those retirees who are unescorted per the definition noted above (*"Those covered retirees that come from an agency that does not cover its active employees in the state program."*), cannot be individually identified if they retired prior to the available 36 month claims data time frame. The retiree claims and eligibility data do not include information in which agency, or agencies, a retiree was associated as an active employee unless the retirement occurred within the last thirty-six months, in which case it is possible to identify only the most recent agency in which that retiree was associated as an active employee before retirement. If the individual retired within the 36 month time frame they could be mapped back to their final active agency by using a time-intensive, manual process. However, this person-by-person identification process would not be able to identify as unescorted or escorted those individuals who retired more than thirty-six months ago, potentially overlooking large numbers of unidentifiable unescorted retirees.)

Service History Information

The active employees of the regional universities, various school boards, and local government agencies are eligible to participate in the KEHP program. Per the Personnel Cabinet, many local government agencies have opted not to participate. The issue is that individual employees within these agencies move from agency to agency as active employees. Thus, a retiree may have some active service attributable to an agency that did provide coverage for its actives through the KEHP program, and some active service attributable to an agency that did not provide coverage to its active employees through the KEHP program. As noted above, the service history of employees while active is not available. Therefore, given that active employees may have worked for both escorted and unescorted retiree-related agencies through the course of their careers, it is not possible with complete assurance to associate historic claims experience with the underlying active employee groups even if the retirement occurred within the last thirty-six months.

Definition of Unescorted Retirees

Further complicating the analysis is differing definitions of unescorted retirees. The definition of unescorted retirees as provided in the prior PwC report dated May 2, 2006, is:

> *Those covered retirees that come from an agency that does not cover its active employees in the state program.*

The Teachers' Retirement System of Kentucky (KTRS) has provided a more expansive definition (per a memorandum dated September 28, 2005) of unescorted retirees:

> *Any pre-Medicare retiree who participates in the Kentucky Employees Health Plan (KEHP), but did not participate in the KEHP during some or all of the time of their employment.*

Each of these definitions relate to the service history of individual retirees. As has been described above, there is insufficient active employment service history information available for individual retirees to apply either of the definitions above.

These different definitions raise a number of issues that complicate the quantification of the costs associated with the unescorted retirees:

- *What is the formal definition of an unescorted retiree?* Confirmation of the definition is necessary to identify all of the current unescorted retirees in the KEHP program.

- *Is this definition concrete, or has it changed in the past?* If the definition has changed over time, it is necessary to identify historic changes in definition and the points in time at which the definition changed. Without this historic trail of the definition, it may not be possible to include anyone currently considered an unescorted retiree who was defined as such under a prior definition. Given the significant difference in the two definitions above, this issue could exclude a number of unescorted retirees currently covered but defined under an older set of criteria.

  In the event that the definition has changed historically, any unescorted retiree covered under a definition more than thirty-six months old possibly could not be identified. To properly define a retiree as an unescorted retiree, information on his/her entire working lifetime would need to be considered.

- *Could the definition change in the future?* If so there will be an ongoing need, similar to that noted above, to maintain (1) the unescorted retiree definition, and (2) the employee work history.

- *How should a "partial" unescorted retiree be treated?* As noted in the KTRS memorandum, University retirees who could have previously been school district employees would create a partial unescorted retiree status (not an unusual situation, per KTRS). The broader issue is certainly <u>any</u> retiree who switched agencies where one agency did participate in the KEHP plan and one did not creates a "partial" unescorted retiree. Complicated actuarial questions are raised regarding the allocation of unescorted retiree costs based on partial unescorted retiree status:

  - <u>Example:</u> If the retired participant worked as an active employee 25 years, 10 of which were for an agency that covered its active employees through the KEHP, and 15 of which were for an agency that covered its active employees through other means, should only 60% (i.e., 15 ÷ 25) of the retiree's costs be considered as being unescorted retiree costs?

  - <u>Example:</u> In the above situation, if the most recent coverage the retiree had as an active employee was provided outside of the KEHP program, should he/she be treated entirely as an unescorted retiree, regardless of the work history? Conversely, if the final active year of the retiree's coverage was provided under the KEHP program, would this retiree be treated as an escorted retiree?

- *Are retirees who voluntarily waived coverage while actives considered unescorted retirees?* If at any time during an active employee's working career he/she waived the KEHP program coverage, under the above KTRS definition this person would be considered an unescorted retiree, irrespective of the active employee agency affiliations. Identification of these individuals would necessitate review of employment records for the entire working career. While an extreme example, what of the person who waives coverage for half of his/her active working career?

CLASSIFYING RETIREES AS ESCORTED OR UNESCORTED

As a result of discussions with the Personnel and Finance and Administration Cabinets on the above issues, the Cabinets indicated that the definition provided in the prior PwC study would continue to apply. Furthermore, the Cabinets indicated that certain retiree groups are largely comprised of unescorted retirees. As such, this analysis (as was the case with the prior analysis) has used as its practical definition of "unescorted retirees" the following, per the direction of these Cabinets:

All covered retirees associated with retiree agencies noted by the Personnel and Finance and Administration Cabinets as consisting largely of retirees who come from an agency that does not cover its active employees in the state program.

It is recognized that the application of this practical definition may treat as an unescorted retiree some retirees who are, in fact, not unescorted, and vice versa. As noted above, however, there is no data-driven approach that can be used to reliably identify, at the individual level, all unescorted retirees.

As such, this analysis looks separately at the retiree claims experience by entire retiree groups, assuming that, within each group, the participants are all either escorted retirees or unescorted retirees, per the direction of the Personnel and Finance and Administration Cabinets. The following non-Medicare eligible retiree assignments were provided to PwC for this analysis:

Retiree Group	Retirees Classification
Judicial Retirement System	Escorted Retirees
KTRS Local School Districts	Escorted Retirees
KTRS Regional Universities[1]	**Unescorted Retirees**
KY Retirement Systems	Escorted Retirees
KY Retirement Systems CERS[2]	**Unescorted Retirees**
KY Retirement Systems KERS	Escorted Retirees
KY Retirement Systems SPRS	Escorted Retirees
KY Teacher Retirement	Escorted Retirees
Legislative Retirement System	Escorted Retirees

[1] *Technical note:* KTRS Regional University retirees are identified via the Thomson Reuters MedStat agency code of 85020.

[2] *Technical note:* KY Retirement Systems CERS retirees are identified via the Thomson Reuters MedStat agency codes of 80020, 80021, 80022, 80023, 80024, and 80025.

A listing at the end of this report provides the assignment for each KEHP Agency Code of:

- Active Employees - Participate in the KEHP program and are included in this analysis per the KLC designation assignment list
- Active Employees - Participate in the KEHP program but are excluded in this analysis per the KLC designation assignment list
- Escorted Retirees
- Unescorted Retirees

Note that the above classifications may or may not be comprised entirely of unescorted retirees. The Personnel and Finance and Administration Cabinets have indicated that the majority in each group are escorted or unescorted retirees as noted. Therefore, this analysis assumes that the above groups properly reflect the split between escorted retirees and unescorted retirees. (It should also be noted that the above groups exclusively include retirees, with no active employee counts.)

STUDY METHODOLOGY

This study is based on the technical definition of unescorted retirees as provided in the prior PwC report dated May 2, 2006, subject to the practical application of that definition to the level of detail available in the claims and enrollment data:

> *Those covered retirees that come from an agency that does not cover its active employees in the state program.*

The claims data reviewed was incurred during the period January 2006 through June 2008 and paid between the dates of January 2006 through August 2008. As there is often a lag between the incurred (or service) date of a claim and the date when it is ultimately adjudicated, payments after June 30, 2008, are included to provide as much complete incurred claims data as possible. While there can be no assurance that all claims that have been incurred in the January 2006 through June 2008 period have been reported and paid by August 31, 2008, actuarial incurred but not reported IBNR claims analyses based on the KEHP program's own claims data indicate the following (approximate) percentages of claims completions:

Covered Group	Coverage Period			
	CY2006	FY2007	CY2007	FY2008
Active Employees	99.99%	99.97%	99.89%	98.75%
Escorted Retirees	99.99%	99.99%	99.96%	99.19%
Unescorted Retirees	99.99%	99.97%	99.86%	99.17%

CY2006, CY2007, and FY2008 claims experience were matched to the underlying agency enrollment. The Per Employee Per Month (PEPM) and Per Member Per Month (PMPM) results for each 12-month measurement period have been developed in aggregate basis across all plan options. Administrative fees were excluded, as were any other non-claims based costs.

STUDY RESULTS

Following are the PMPM and PEPM claims cost relationships between groups:

Per Employee Per Month Ratio of Unescorted Retiree Claims Costs to Benchmark Group				
Relationship	Measurement Period			
	CY2006	FY2007	CY2007	FY2008
Unescorted Retirees *vs.* Actives Only	1.437	1.440	1.433	1.422
Unescorted Retirees *vs.* Escorted Retirees Only	1.064	1.056	1.044	1.038
Unescorted Retirees *vs.* Actives + Escorted Retirees	1.361	1.345	1.325	1.310
Unescorted Retirees *vs.* Total	1.325	1.310	1.292	1.278
Actives + Escorted Retirees *vs.* Total	0.973	0.974	0.975	0.976

Per Member Per Month Ratio of Unescorted Retiree Claims Costs to Benchmark Group				
Relationship	Measurement Period			
	CY2006	FY2007	CY2007	FY2008
Unescorted Retirees *vs.* Actives Only	1.653	1.661	1.656	1.644
Unescorted Retirees *vs.* Escorted Retirees Only	0.957	0.948	0.935	0.926
Unescorted Retirees *vs.* Actives + Escorted Retirees	1.510	1.494	1.474	1.458
Unescorted Retirees *vs.* Total	1.459	1.444	1.426	1.411
Actives + Escorted Retirees *vs.* Total	0.966	0.967	0.967	0.968

The results of this study are consistent over the 30-month data period reviewed. The differences between PEPM and PMPM costs are explained by the fact that the average family size per contract is larger for actives than it is for either the escorted retirees or the unescorted retirees.

The following comparisons focus on the FY2008 results.

Comparison of Unescorted Retirees *versus* Active Employees

On a FY2008 PMPM basis, the claims costs for the unescorted retirees and their dependents were approximately 65.3% higher than that for the active employees and their dependents.

Similarly on a FY2008 PEPM contract basis the claims costs for the unescorted retirees and their dependents were approximately 43.7% higher than that for the active employees and their dependents.

Comparison of Unescorted Retirees *versus* Escorted Retirees

On a FY2008 PMPM basis the claims costs for the unescorted retirees and their dependents were approximately 4.3% lower than that for escorted retirees and their dependents. On a FY2008 PEPM contract basis the claims costs for the unescorted retirees and their dependents were approximately 6.4% higher than that for the escorted retirees and their dependents.

It is important to note that the difference in PEPM and PMPM claims between those retirees identified as unescorted and those retirees identified as escorted has remained largely unchanged throughout the analysis time periods of calendar year 2006 through fiscal year 2008 (and generally consistent with the results of the prior study), and that the PEPM and PMPM claims between these two retiree groups have been generally consistent, indicating that the issue of the subsidy is not so much one of unescorted retirees, but of retirees in general.

As a result, regardless of the definition used to identify unescorted retirees (technical or practical), the results of any actuarial analysis comparing active employee results to retiree results will demonstrate and quantify the degree active employees are subsidizing retirees, both escorted and unescorted.

Comparison of Unescorted Retirees *versus* Active Employees + Escorted Retirees

On a FY2008 PMPM basis the claims costs for the unescorted retirees and their dependents were approximately 51.0% higher than that for the active employees and escorted retirees and their dependents. Similarly on a FY2008 PEPM contract basis the claims costs for the unescorted retirees and their dependents were approximately 36.1% higher than that for the active employees and escorted retirees, and their dependents combined. **This difference in claims cost reflects the subsidization of the unescorted retirees by the actives and escorted retirees.**

Comparison of Unescorted Retirees *versus* All

On a FY2008 PMPM basis the claims costs for the unescorted retirees and their dependents were approximately 45.9% higher than that for the entire group (active employees and their dependents, escorted retirees and their dependents, and unescorted retirees and their dependents). Similarly on a FY2008 PEPM basis the claims costs for the unescorted retirees and their dependents were approximately 32.5% higher than that for the entire group.

Active Employees + Escorted Retirees *versus* All

When comparing the FY2008 costs of the active employees plus the escorted retirees against the entire group, the PMPM and PEPM costs for the actives and escorted retirees were 96.8% and 97.6%, respectively, of the claims costs of the entire group (including the unescorted retirees). **Therefore, the costs of providing coverage to the actives and escorted retirees would be 3.2% lower (PMPM basis) and 2.4% lower (PEPM basis) if the unescorted retirees were not included in the KEHP program.**

The KEHP program is subsidizing not only the unescorted retirees, but also the active employees of agencies that provide coverage outside of the KEHP program but cover their non-Medicare eligible retirees under the KEHP program. In other words, the active employees of agencies that cover retirees in the KEHP program but provide coverage for actives outside of the program are realizing a lower cost given that they are not subsidizing the cost of the retirees of their own group. It is not possible to quantify the extent of this subsidization as no cost or enrollment information is available for those active employee populations that currently provide coverage outside of KEHP.

The following chart presents the total claims incurred by the unescorted group in the 12-month measurement periods analyzed in this report. The average annual increase in claims during these periods was approximately 6.4% (PMPM basis), and 7.1% (PEPM basis).

Total Claims By Group				
Unescorted Retiree Claims Metric	Measurement Period			
	CY2006	FY2007	CY2007	FY2008
Total Claims ($Millions)	$97.2	$104.0	$112.0	$118.6
Total Subsidized Amount ($Millions)	$36.5	$37.0	$37.3	**$37.2**
PMPM Claims	$501.00	$517.91	$536.83	$549.87
PEPM Claims	$732.62	$759.27	$789.12	$810.85
PMPM Subsidized Amount	$169.30	$171.28	$172.72	**$172.63**
PEPM Subsidized Amount	$194.02	$194.84	$193.63	**$191.87**

As shown above, in FY2008, unescorted retirees costs were subsidized by KEHP actives and escorted retirees in the total amount of $37.2 million when analyzed on a PMPM basis. This $37.2 million subsidy translates to an unescorted retiree FY2008 subsidy amount of $172.63 PMPM.

When analyzed on a PEPM basis, the $37.2 million subsidy translates to an unescorted retiree FY2008 subsidy amount of $191.87 PEPM. The reason that the subsidy amount differs on a PEPM vs. PMPM basis is because the family sizes of the actives and escorted retirees differ from that of the unescorted retirees (i.e., there are different average number of members per employee ratios for the groups).

CONSIDERATIONS AND OPTIONS

Following are several approaches for addressing the subsidy provided to the unescorted retirees. The considerations and options discussed below do not address restrictions that may exist due to current Commonwealth of Kentucky statutes, and may not be feasible, in some cases, without changes to some existing statutes.

1. Make no changes to the current programs and pricing. This approach would require no immediate action. The concern is that the portion of the covered population comprised by retirees is growing, decreasing the percentage of the population that is the active employee base upon which the subsidies are provided. As the retiree population grows (whether it be the unescorted retirees, the escorted retirees, or both), health care trend would be expected to continue at levels in excess of market rates. This will have a ripple effect:

    - As costs increase in excess of expected healthcare trend more agencies may see the cost benefit of moving active employees out of the KEHP program while continuing to cover non-Medicare eligible retirees under the KEHP program.

    - This would further erode the active base beyond what is currently projected, and accelerate cost increases.

    - This could ultimately produce untenable costs for the KEHP program, effectively pricing it out of the market.

2. Prohibit unescorted retirees from participating in the KEHP program. Structure the KEHP program such that coverage for non-Medicare eligible retirees would only be available if the corresponding active employee group was covered by the program. While this approach would eliminate the unescorted retiree group, it may be difficult to administer and/or enforce given the previously-noted migration from agency to agency of some active employees.

3. Charge higher premiums for unescorted retirees. The Cabinet could establish a two-tier pricing arrangement whereby the active employees and escorted retirees would have one set of rates that would be developed on an experience basis for those groups, while the unescorted retirees would have a separate set of rates that would be developed based on

their own experience. This study estimated the differential in the two sets of rates as being a load of 45.8% for unescorted retirees on a PMPM basis, or a load of 31.0% for unescorted retirees on a PEPM basis. This cost neutral approach would also possibly have the effect of enhancing the attractiveness of the KEHP program rates to agencies currently not covering their actives and reducing or eliminating the incentive for unescorted retirees to participate in the KEHP program.

4. Charge separate premiums for actives versus all non-Medicare eligible retirees. This approach is an expansion of the previous option, and would eliminate the active population's subsidy provided to all enrolled retirees.

5. Charge each agency separately for its own covered participant population. While actuarially more equitable than the above approaches, this approach could introduce some issues of credibility for pricing purposes. In other words, the underlying population for an agency may not be large enough to have claims data robust enough for projection purposes. If this occurs, then additional methods would be needed to adjust for this lack of critical mass, and could introduce new issues of subsidization.

6. Create a separate health plan option (with its own rates) for the unescorted retirees. Unlike approach #3 above, which provided the same health options to unescorted retirees as are offered to actives and escorted retirees, this approach would be based on a unique plan (or set of plans) available only to the unescorted retirees. This would allow the KEHP program to separately establish plan design provisions and rates for the unescorted retirees versus the active/escorted retiree groups, potentially providing better ability to manage costs.

7. Reduce the benefits provided to the unescorted retirees so that the rates match those applicable to the active/escorted retiree groups. This is a specific example of approach #6. Since this analysis has excluded the costs associated with the KRS-defined Excluded Active employee agencies, an estimate of the benefit change for this approach has not been determined. However, such an approach would create a two-tier benefit design system that would be more complicated and costly to administer and communicate, and could change year-to-year as the cost differentials or even the enrollment patterns between the escorted group and the other groups changed. This approach also assumes that the benefits between the Included Active group and the Excluded Active group would remain the same.

8. Assess a surcharge to the agencies that do not cover active employees in plan. This approach could reduce or eliminate the incentive for agencies to cover their retirees under the KEHP plan while covering actives independently.

STUDY METHODOLOGY CAVEATS

The caveats below pertain to the study methodology. In addition to the caveat discussed in the body of the report under the "Study Limitations" section please note the following explanations:

Credibility

In actuarial analyses the term "credibility" is used with respect to the claims and enrollment data. Credibility does not refer to whether or not the data are accurate. The presumption is that all data provided are accurate and complete. In actuarial discussions "credibility" refers to the extent to which it is felt that there is sufficient "critical mass" to the data from which valid conclusions can be drawn. In developing the PMPM and PEPM measures, credibility measures have been determined based on the 1988 Transaction of the Society of Actuaries (vol. XL) study, which assesses levels of credibility based on exposure counts (i.e., number of covered lives) for the active and non-Medicare eligible retired employee coverage groups. The following credibility formula was used from this study:

$$\frac{k_1 + (n-1)*k_2}{1 + (n-1)*k_3}$$

Where: $k_1 = 0.0250$
$k_2 = 0.0050$
$k_3 = 0.0045$
n = number of lives

Any population with over 2,000 lives is considered 100% actuarially credible, and can be actuarially relied upon for purposes of estimating health care costs prospectively. The sizes of the unescorted retiree, escorted retiree, and active populations are all sufficiently large that there were no issues of less than full credibility of the data.

Geographic, Demographic, and Benefit Differences

Active and non-Medicare eligible retiree claims experience was compared to average claims costs. Where enrollment patterns in the various benefit options differed between actives and escorted retirees and unescorted retirees due to geographic location, family size (in the case of PEPM measures), and/or differences in benefit plan provisions, some of the cost differences could be explained by these different enrollment patterns. Our study did not attempt to adjust for these different enrollment patterns. Ultimately, the issue of subsidization is based on the extent to which these enrollment differences and cost differences are present. To smooth the data to account for expected differences by geography, demographics, and plan provisions could introduce more subsidization.

TABLES

The tables that follow present claims and enrollment information by active versus escorted retiree versus unescorted retiree. Note only data from FY2008 are included in this appendix.

Table 1
Counts of Actives, Escorted Retirees, and Unescorted Retirees

Average Monthly Number of Covered Employees or Retirees			
FY2008	**Included Actives**	**Retirees**	
		Escorted	Unescorted
Members	72,894	38,306	17,978
Employees	42,748	29,128	12,192

Table 2
FY2008 Claims for Actives, Escorted Retirees, and Unescorted Retirees

Claims Incurred By Members			
FY2008	**Included Actives**	**Retirees**	
		Escorted	**Unescorted**
Total	$292,568,000	$273,042,000	$118,627,000

Note: The claims data shown here reflects claims incurred in FY2008, and paid between July 1, 2007, and August 31, 2008. Also included in the FY2008 claims data here are estimates of the incurred but not reported (IBNR) claims incurred in FY2008 but not yet paid as of August 31, 2008.

Table 3
FY2008 PMPM and PEPM Claims for Actives, Escorted Retirees, and Unescorted Retirees

Average Monthly Claims Incurred By Member					
FY2008	**Included Actives**	**Retirees**		**Actives + Escorted**	**Total**
		Escorted	**Unescorted**		
PMPM	$334.47	$594.00	$549.87	$377.24	$389.67
PEPM	$570.33	$781.16	$810.85	$618.98	$634.24

Note: The claims data shown here reflects claims incurred in FY2008, and paid between July 1, 2007, and August 31, 2008. Also included in the FY2008 claims data here are estimates of the incurred but not reported (IBNR) claims incurred in FY2008 but not yet paid as of August 31, 2008.

AGENCY LISTING & FY2008 EMPLOYEE AND MEMBER ENROLLMENT COUNTS

The table that follows provides an agency-by-agency listing of all KEHP agency codes used to identify:

- The active employee groups included in this analysis,
- The active employee groups identified by KRS to be excluded from this analysis (subject to the issue noted in the body of this report regarding the attempt to match the KRS agency list per its coding scheme against the coding scheme maintained by KEHP and Thomson Reuters' MedStat data warehouse to which PwC has access,
- The retiree groups defined as escorted per the practical definition noted in this report, and
- The retiree groups defined as unescorted per the practical definition noted in this report.

Average monthly employee and member KEHP program enrollment counts for the FY2008 are included.

Note that only data from FY2008 are included in this appendix. While additional KEHP agency codes are in place, they have been omitted from this list in cases where no employees or members were listed as being associated with that agency at any point in FY2008.

KEHP Agency Code	Agency Name	Grouping				FY2008 Employees		FY2008 Members	
		Actives		Early Retirees					
		Included	Excluded	Escorted	Unescorted	Actives	Early Retirees	Actives	Early Retirees
00001	ADAIR BOARD OF EDUCATION		X			364		639	
00005	ALLEN BOARD OF EDUCATION		X			315		619	
00006	ANCHORAGE BOARD OF EDUCATION		X			52		117	
00011	ANDERSON BOARD OF EDUCATION		X			340		674	
00012	ASHLAND INDEPENDENT	X				322		506	
00013	AUGUST INDEPENDENT	X				37		61	
00015	BALLARD BOARD OF EDUCATION		X			147		270	
00016	BARBOURVILLE INDEPENDENT	X				60		136	
00017	BARDSTOWN INDEPENDENT		X			240		440	
00021	BARREN BOARD OF EDUCATION		X			497		961	
00025	BATH BOARD OF EDUCATION		X			229		433	
00026	BEECHWOOD INDEPENDENT	X				64		128	
00031	BELL BOARD OF EDUCATION		X			423		730	
00032	BELLEVUE INDEPENDENT SCHOOLS		X			80		124	
00034	BEREA INDEPENDENT		X			106		207	
00035	BOONE BOARD OF EDUCATION		X			1,294		2,350	
00041	BOURBON CO BOARD OF EDUCATION		X			283		512	

KEHP Agency Code	Agency Name	Grouping				FY2008 Employees		FY2008 Members	
		Actives		Early Retirees					
		Included	Excluded	Escorted	Unescorted	Actives	Early Retirees	Actives	Early Retirees
00042	BOWLING GREEN INDEPENDENT		X			423		749	
00045	BOYD BOARD OF EDUCATION		X			345		584	
00051	BOYLE BOARD OF EDUCATION		X			282		540	
00055	BRACKEN CO BOARD OF EDUCATION		X			102		183	
00061	BREATHITT CO BOARD OF ED		X			359		590	
00065	BRECKINRIDGE CO BD OF ED		X			293		539	
00071	BULLITT CO BOARD OF ED		X			993		1,772	
00072	BURGIN INDEPENDENT		X			44		90	
00075	BUTLER CO BOARD OF EDUCATION		X			236		442	
00081	CALDWELL CO BOARD OF ED		X			227		437	
00085	CALLOWAY CO BOARD OF ED		X			381		654	
00091	CAMPBELL CO BOARD OF ED		X			406		743	
00092	CAMPBELLSVILLE INDEPENDENT		X			143		271	
00095	CARLISLE CO BOARD OF ED		X			87		167	
00101	CARROLL CO BOARD OF EDUCATION		X			218		371	
00105	CARTER CO BOARD OF EDUCATION		X			579		886	
00111	CASEY CO BOARD OF EDUCATION		X			313		591	
00113	CAVERNA INDEPENDENT		X			86		161	
00115	CHRISTIAN CO BOARD OF ED		X			953		1,577	
00121	CLARK CO BOARD OF EDUCATION		X			519		916	
00125	CLAY CO BOARD OF EDUCATION		X			584		993	
00131	CLINTON CO BOARD OF EDUCATION		X			242		442	
00132	CLOVERPORT INDEPENDENT		X			37		60	
00133	CORBIN INDEPENDENT SCHOOLS	X				224		423	
00134	COVINGTON INDEPENDENT BD OF ED		X			550		850	
00135	CRITTENDEN CO BOARD OF ED		X			146		272	
00141	CUMBERLAND CO BOARD OF ED		X			139		289	
00143	DANVILLE INDEPENDENT	X				233		393	
00145	DAVIESS CO BOARD OF EDUCATION		X			1,080		1,952	
00146	DAWSON SPRINGS INDEPENDENT		X			60		125	
00147	DAYTON INDEPENDENT SCHOOL		X			89		147	
00149	EAST BERNSTADT INDEPENDENT	X				54		99	
00151	EDMONSON CO BOARD OF EDUCATION		X			260		471	
00152	ELIZABETHTOWN INDEPENDENT	X				169		341	
00155	ELLIOTT CO BOARD OF EDUCATION		X			145		248	
00156	EMINENCE INDEPENDENT SCHOOLS	X				65		150	
00157	ERLANGER -ELSMERE BD OF ED		X			195		325	
00161	ESTILL CO BOARD OF EDUCATION		X			253		442	
00162	FAIRVIEW INDEPENDENT	X				68		108	
00165	FAYETTE CO BOARD OF EDUCATION		X			3,879		6,660	
00171	FLEMING CO BOARD OF EDUCATION		X			289		512	
00175	FLOYD CO BOARD OF EDUCATION		X			758		1,231	
00176	FT THOMAS INDEPENDENT	X				193		347	

KEHP Agency Code	Agency Name	Grouping				FY2008 Employees		FY2008 Members	
		Actives		Early Retirees					
		Included	Excluded	Escorted	Unescorted	Actives	Early Retirees	Actives	Early Retirees
00177	FRANKFORT INDEPENDENT		X			96		190	
00181	FRANKLIN CO BOARD OF EDUCATION		X			623		1,133	
00185	FULTON CO BOARD OF EDUCATION		X			82		136	
00186	FULTON INDEPENDENT		X			63		128	
00191	GALLATIN CO BOARD OF EDUCATION		X			158		266	
00195	GARRARD CO BOARD OF EDUCATION		X			300		492	
00197	GLASGOW INDEPENDENT	X				183		394	
00201	GRANT CO BOARD OF EDUCATION		X			358		628	
00205	GRAVES CO BOARD OF EDUCATION		X			498		889	
00211	GRAYSON CO BOARD OF EDUCATION		X			435		803	
00215	GREEN CO BOARD OF EDUCATION		X			218		401	
00221	GREENUP CO BOARD OF EDUCATION		X			325		514	
00225	HANCOCK CO BOARD OF EDUCATION		X			146		275	
00231	HARDIN CO BOARD OF EDUCATION		X			1,266		2,315	
00235	HARLAN CO BOARD OF EDUCATION		X			533		848	
00236	HARLAN INDEPENDENT	X				83		155	
00241	HARRISON CO BOARD OF EDUCATION		X			272		491	
00245	HART CO BOARD OF EDUCATION		X			302		573	
00246	HAZARD INDEPENDENT BD OF ED		X			95		152	
00251	HENDERSON CO BOARD OF ED		X			755		1,261	
00255	HENRY CO BOARD OF EDUCATION		X			201		335	
00261	HICKMAN CO BOARD OF EDUCATION		X			97		186	
00265	HOPKINS CO BOARD OF EDUCATION		X			887		1,450	
00271	JACKSON CO BOARD OF EDUCATION		X			343		583	
00272	JACKSON INDEPENDENT		X			47		95	
00275	JEFFERSON CO BOARD OF ED		X			10,194		16,620	
00276	JENKINS INDEPENDENT SCHOOLS	X				76		112	
00281	JESSAMINE CO BOARD OF ED		X			864		1,498	
00285	JOHNSON CO BOARD OF EDUCATION		X			430		766	
00291	KENTON CO BOARD OF EDUCATION		X			1,031		1,824	
00295	KNOTT CO BOARD OF EDUCATION		X			319		501	
00301	KNOX CO BOARD OF EDUCATION		X			603		1,081	
00305	LARUE CO BOARD OF EDUCATION		X			223		425	
00311	LAUREL CO BOARD OF EDUCATION		X			928		1,697	
00315	LAWRENCE CO BOARD OF EDUCATION		X			281		429	
00321	LEE CO BOARD OF EDUCATION		X			160		277	
00325	LESLIE CO BOARD OF EDUCATION		X			251		394	
00331	LETCHER CO BOARD OF EDUCATION		X			426		721	
00335	LEWIS CO BOARD OF EDUCATION		X			304		533	
00341	LINCOLN CO BOARD OF EDUCATION		X			547		966	
00345	LIVINGSTON CO BOARD OF ED		X			161		296	
00351	LOGAN CO BOARD OF EDUCATION		X			410		689	

KEHP Agency Code	Agency Name	Grouping: Actives: Included	Grouping: Actives: Excluded	Grouping: Early Retirees: Escorted	Grouping: Early Retirees: Unescorted	FY2008 Employees: Actives	FY2008 Employees: Early Retirees	FY2008 Members: Actives	FY2008 Members: Early Retirees
00354	LUDLOW INDEPENDENT	X				61		116	
00361	LYON CO BOARD OF EDUCATION		X			103		202	
00365	MADISON CO BOARD OF EDUCATION		X			1,007		1,873	
00371	MAGOFFIN CO BOARD OF ED		X			285		447	
00375	MARION BOARD OF EDUCATION		X			317		595	
00381	MARSHALL CO BOARD OF EDUCATION		X			499		944	
00385	MARTIN CO BOARD OF EDUCATION		X			320		488	
00391	MASON CO BOARD OF EDUCATION		X			270		479	
00392	MAYFIELD INDEPENDENT		X			199		339	
00395	MCCRACKEN CO BOARD OF ED		X			604		1,115	
00401	MCCREARY CO BOARD OF EDUCATION		X			449		755	
00405	MCLEAN BOARD OF EDUCATION		X			188		312	
00411	MEADE CO BOARD OF EDUCATION		X			408		818	
00415	MENIFEE CO BOARD OF EDUCATION		X			156		280	
00421	MERCER CO BOARD OF EDUCATION		X			324		622	
00425	METCALFE CO BOARD OF ED		X			196		381	
00426	MIDDLESBORO INDEPENDENT		X			170		291	
00431	MONROE CO BOARD OF EDUCATION		X			306		554	
00435	MONTGOMERY CO BOARD OF ED		X			460		784	
00436	MONTICELLO IND BOARD OF ED		X			108		223	
00441	MORGAN CO BOARD OF EDUCATION		X			266		461	
00445	MUHLENBERG CO BOARD OF ED		X			597		987	
00446	MURRAY INDEPENDENT BD OF ED	X				197		340	
00451	NELSON CO BOARD OF EDUCATION		X			453		793	
00452	NEWPORT INDEPENDENT BD OF ED		X			257		422	
00455	NICHOLAS COUNTY SCHOOLS	X				126		229	
00461	OHIO BOARD OF EDUCATION		X			447		758	
00465	OLDHAM CO BOARD OF EDUCATION		X			1,020		1,866	
00471	OWEN CO BOARD OF EDUCATION		X			187		372	
00472	OWENSBORO INDEPENDENT BD OF ED		X			531		860	
00475	OWSLEY CO BOARD OF EDUCATION		X			146		240	
00476	PADUCAH INDEPENDENT BD OF ED		X			342		571	
00477	PAINTSVILLE INDEP BD OF ED		X			99		179	
00478	PARIS INDEPENDENT SCHOOLS	X				93		151	
00481	PENDLETON CO BOARD OF ED		X			277		543	
00485	PERRY CO BOARD OF EDUCATION		X			592		912	
00491	PIKE CO BOARD OF EDUCATION		X			1,084		1,769	
00492	PIKEVILLE INDEPENDENT BD OF ED		X			107		188	
00493	PINEVILLE INDEPENDENT BD OF ED	X				63		120	
00495	POWELL CO BOARD OF EDUCATION		X			287		492	
00496	PROVIDENCE INDEPENDENT		X			4		7	

KEHP Agency Code	Agency Name	Grouping				FY2008 Employees		FY2008 Members	
		Actives		Early Retirees					
		Included	Excluded	Escorted	Unescorted	Actives	Early Retirees	Actives	Early Retirees
00501	PULASKI CO BOARD OF EDUCATION		X			954		1,769	
00502	RACELAND - WORTHINGTING IND	X				86		153	
00505	ROBERTSON CO BOARD OF ED		X			49		83	
00511	ROCKCASTLE CO BOARD OF ED		X			348		636	
00515	ROWAN CO BOARD OF EDUCATION		X			353		619	
00521	RUSSELL CO BOARD OF EDUCATION		X			425		781	
00522	RUSSELL INDEPENDENT	X				159		289	
00523	RUSSELLVILLE INDEPENDENT		X			116		194	
00524	SCIENCE HILL INDEPENDENT	X				49		101	
00525	SCOTT CO BOARD OF EDUCATION		X			669		1,212	
00531	SHELBY CO BOARD OF EDUCATION		X			559		998	
00533	SILVER GROVE INDEPENDENT	X				32		56	
00535	SIMPSON BOARD OF EDUCATION		X			323		597	
00536	SOMERSET INDEPENDENT	X				177		330	
00537	SOUTHGATE INDEPENDENT	X				15		29	
00541	SPENCER CO BOARD OF EDUCATION		X			233		438	
00545	TAYLOR CO BOARD OF EDUCATION		X			276		516	
00551	TODD CO BOARD OF EDUCATION		X			253		461	
00555	TRIGG CO BOARD OF EDUCATION		X			231		451	
00561	TRIMBLE CO BOARD OF EDUCATION		X			133		226	
00565	UNION CO BOARD OF EDUCATION		X			292		467	
00567	WALTON VERONA INDEPENDENT	X				92		201	
00571	WARREN CO BOARD OF EDUCATION		X			1,224		2,166	
00575	WASHINGTON CO BOARD OF ED	X				177		318	
00581	WAYNE CO BOARD OF EDUCATION		X			384		646	
00585	WEBSTER CO BOARD OF EDUCATION		X			263		415	
00586	WEST POINT INDEP BD OF ED	X				11		13	
00591	WHITLEY CO BAORD OF EDUCATION		X			630		1,049	
00592	WILLIAMSBURG INDEPENDENT	X				91		155	
00593	WILLIAMSTOWN INDEPENDENT	X				68		140	
00595	WOLFE CO BOARD OF EDUCATION		X			179		322	
00601	WOODFORD CO BOARD OF ED		X			350		636	
00616	OHIO VALLEY EDUCATIONAL COOP		X			102		187	
00622	KY VALLEY EDUCATION		X			39		59	
00630	WEST KY EDUCATION COOP	X				49		87	
00700	KY EDUCATION DEV COOP		X			73		126	
00701	NORTHERN KY COOP		X			64		107	
00703	GREEN RIVER REGIONAL EDUC COOP	X				16		21	
00704	CENTRAL KY SPE ED COOP	X				7		12	
10005	KENTUCKY GENERAL ASSEMBLY	X				75		154	
10010	LEGISLATIVE RESEARCH COMM	X				309		514	
20020	JUDICAL FORM RETIREMENT SYSTEM	X				2		2	
20025	ADMIN OFFICE OF THE COURTS	X				2,765		4,479	
31030	UNIFIED PROSECUTORIAL SYSTEM	X				728		1,412	

KEHP Agency Code	Agency Name	Grouping: Actives		Grouping: Early Retirees		FY2008 Employees		FY2008 Members	
		Included	Excluded	Escorted	Unescorted	Actives	Early Retirees	Actives	Early Retirees
31035	DEPT OF AGRICULTURE	X				243		426	
31040	ATTORNEY GENERAL	X				160		308	
31045	AUDITOR OF PUBLIC ACCOUNTS	X				109		184	
31066	ELECTION OF FIANCE	X				12		19	
31070	GOVERNORS OFFICE	X				42		60	
31074	DEPT OF VETERANS AFFAIRS	X				636		998	
31076	MILITARY AFFAIRS COMMISSION	X				2		5	
31082	KY INFRASTRUCTURE AUTHORITY	X				11		23	
31085	LT GOVERNORS OFFICE	X				2		6	
31089	AGRICULTURAL DEVELOPMENT BOARD	X				13		20	
31094	OFFICE OF HOMELAND SECURITY	X				15		22	
31095	MILITARY AFFAIRS	X				428		637	
31097	OFFICE OF MINORITY EMPOWERMENT	X				2		3	
31098	GOVERNORS SCHOLAR	X				2		4	
31099	OFFICE OF FAITH AND COMMUNITY	X				2		2	
31100	KY RETIREMENT SYSTEMS	X				177		349	
31110	OFFICE OF SEC TO EXEC. CAB	X				1		3	
31112	DEPT OF LOCAL GOVERMENT	X				46		89	
31120	SECRETARY OF STATE	X				27		43	
31125	TREASURY	X				22		38	
31150	BOARD OF ACCOUNTANCY	X				2		4	
31155	BOARD OF AUCTIONEERS	X				2		4	
31165	BOARD OF BARBERING	X				3		3	
31170	BOARD OF CHIROPRATIC EXAMINERS	X				3		7	
31180	BOARD OF DENTISTRY	X				3		4	
31185	BOARD OF ELECTIONS	X				13		25	
31190	BD OF EMBALMERS & FUNERAL DIR	X				4		6	
31200	BD OF EXAM OF REG ARCHITECTS	X				4		4	
31205	BD OF LANDSCAPE ARCHITECTS	X				0		1	
31225	BD OF HAIRDRESSERS & COSM	X				12		16	
31245	BOARD OF MEDICAL LICENSURE	X				10		22	
31250	BD OF NURSING ED & REG	X				36		74	
31260	BD OF OPTOMETRIC EXAMINERS	X				1		1	
31263	BD OF RESPIRATORY CARE	X				1		1	
31268	PERSONNEL BOARD	X				4		10	
31270	BOARD OF PHARMACY	X				5		15	
31275	BD OF PHYSICAL THERAPIST	X				2		3	
31284	REAL ESTATE APPRAISERS BOARD	X				2		3	
31290	BD OF PROFFESSIONAL ENGINEERS	X				8		19	
31345	SCHOOL FACILITIES CONST COM	X				2		6	
31354	EXECUTIVE BRANCH ETHICS COMM	X				3		6	
31370	HUMAN RIGHTS COMMISSION	X				29		54	

KEHP Agency Code	Agency Name	Grouping: Actives – Included	Grouping: Actives – Excluded	Grouping: Early Retirees – Escorted	Grouping: Early Retirees – Unescorted	FY2008 Employees – Actives	FY2008 Employees – Early Retirees	FY2008 Members – Actives	FY2008 Members – Early Retirees
31395	REAL ESTATE COMMISSION	X				14		23	
31400	COMMISSION ON WOMEN	X				3		3	
31765	GOVS OFFICE POLICY & MGT	X				27		53	
31855	OFFICE OF ENERGY POLICY	X				12		20	
35605	OFFICE OF THE SECRETARY	X				96		158	
35607	OFFICE OF GENERAL COUNCIL	X				46		88	
35609	OFFICE OF SUPPORT SERVICES	X				53		87	
35615	DEPARTMENT OF AVIATION	X				19		36	
35616	TRANS OFC OF PERSONNEL MGT	X				27		54	
35617	OFFICE OF INFO TECHNOLOGY	X				32		59	
35621	DIVISION OF TRAFIC SAFETY	X				47		75	
35625	DEPT OF HIGHWAYS	X				3,532		6,033	
35628	TRAN DEPT INTRGOVMNTL PROGRAMS	X				26		44	
35630	DEPT OF VEHICLE & REGULATIONS	X				170		277	
36635	EDEV-OFFICE OF THE SECRETARY	X				29		64	
36637	DEPT OF JOB DEVELOPMENT	X				8		11	
36638	DEPT OF FINANCIAL INCENTIVES	X				15		33	
36639	DEPT COMMUNITY DEVELOPMENT	X				32		59	
36644	EDEV OFF OF ADMIN & SUP	X				5		8	
39075	HIGHER ED ASSISTANCE AUTH	X				74		130	
39079	FN&A COMMONWEALTH OFF OF TECH	X				345		658	
39084	KY RIVER AUTHORITY	X				7		10	
39103	FN&A- OFFICE OF PVAS	X				560		906	
39130	FN&A DEPT OF REVENUE	X				705		1,103	
39750	F&A OFFICE OF THE SECRETARY	X				150		267	
39758	OFFICE OF THE CONTROLLER	X				70		108	
39785	DEPT OF FACILITIES MGNT	X				242		403	
45470	KCTCS	X				3,020		5,310	
50235	COMM BD KENTUCKY STATE FAIR	X				238		353	
50410	COMM COUNCIL KY HERITAGE	X				17		30	
50529	COMM CONUNCIL KY ARTS	X				13		28	
50550	COMM KY HISTORICL SOCIETY	X				62		91	
50660	COMM DEPT OF FISH & WILDLIFE	X				393		749	
50665	COMM KY HORSE PARK	X				67		111	
50670	COMM DEPT OF PARKS	X				972		1,383	
50850	COMM OFFICE OF THE SECRETARY	X				34		65	
50852	COMM KY ARTISANS CTR AT BEREA	X				22		27	
50860	COMM DEPT OF TOURISM	X				47		65	
51183	EDUC-BD EDUC PROFESSIONAL STDS	X				22		41	
51340	EDUC- COMM- DEAF & HARD HEAR	X				11		17	
51407	EDUC-COUNCIL KY ENVIRONMTL ED	X				1		1	
51415	EDUC- COUNCIL POST SECOND ED	X				66		120	

KEHP Agency Code	Agency Name	Grouping: Actives		Grouping: Early Retirees		FY2008 Employees		FY2008 Members	
		Included	Excluded	Escorted	Unescorted	Actives	Early Retirees	Actives	Early Retirees
51530	EDUC- OFFICE OF SECRETARY	X				88		151	
51531	EDUC- DEPT WORKFORCE INVEST	X				1,355		2,345	
51540	EDUC- DEPT OF EDUCATION	X				496		886	
51545	EDUC- KY EDUC TV AUTHORITY	X				136		265	
51555	EDUC- DEP LIBRARIES & ARCHIVES	X				112		177	
52350	EPPC-COMM-ENVIRONMENTL QUALITY	X				3		5	
52375	EDUC- COM- KY NATURE PRESERVES	X				19		29	
52380	EPPC- COMM- KY OCC SAFE & HLTH	X				3		6	
52423	EPPC- MINE SAFETY REVIEW COMM	X				7		9	
52424	EPPC-MINE SAFETY REVIEW COMMIS	X				1		1	
52569	EPPC- OFFICE OF THE SECRETARY	X				158		286	
52590	EPPC DEPT FOR ENVIRON PROTE	X				673		1,175	
52595	EPPC- DEPT NATURAL RESOURCES	X				646		1,162	
52695	EPPC- DEPT OF PUB PROTECTION	X				596		1,086	
52920	EPPC- DEPT OF LABOR	X				277		490	
52930	WORKERS COMP FUNDING COM	X				10		17	
53721	H&FS- OFFICE OF THE SECRETARY	X				340		617	
53722	GOVERNORS OF WELLNESS & PHYSI	X				8		9	
53723	H&FS- OFFICE OF INSPECTOR GENL	X				215		372	
53724	H&FS-OFF OF HEALTH POLICY	X				8		17	
53725	DEPT FOR AGING & INDE LIVING	X				26		34	
53726	H&FS DEP DISABIL DETERM SERV	X				318		502	
53728	H&FS- DEPT FOR PUBLIC HEALTH	X				294		469	
53729	H&FS-DEP MNTL HTH/MNTL RET SRV	X				985		1,466	
53730	H&FS DEPT HUMAN SUPPORT SRVS	X				18		29	
53731	H&FS OFFICE OF OMBUDSMAN	X				68		114	
53736	H&FS-DEPT COMMUNITY BASED SRVS	X				3,752		6,129	
53746	H&FS- DEPT FOR MEDICAID SERVS	X				104		170	
53767	H&FS-COM CHLD W/SPEC HLTH NEED	X				121		216	
54500	J&PS OFFICE OF THE SECRETARY	X				69		133	
54502	J&PS- DEPT OF KY VEH ENFORCE	X				202		399	
54515	J&PS- DEPT OF PUBLIC ADVOCACY	X				399		688	
54520	J&PS- DEPT OF KY STATE POLICE	X				1,374		2,667	
54523	J&PS- DEPT OF JUVENILE JUSTICE	X				1,233		2,153	
54525	J&PS-DEPT CRIM JUSTICE TRAIN	X				85		139	
54527	J&PS- DEPT OF CORRECTIONS	X				3,234		5,222	
55790	PERSONNEL CABINET OFFIC OF SEC	X				69		128	
55793	DEPT FOR PERSONNEL ADMINISTRAT	X				65		110	
55794	DEPT FOR EMPLOYEE INSURANCE	X				33		74	
80000	KRS-KY RETIREMENT SYSTEMS			X			6		63
80010	KY RETIREMENT SYSTEMS KERS			X			13,035		17,505
80020	CERS - OTHER AGENCIES				X		129		176

KEHP Agency Code	Agency Name	Grouping: Actives: Included	Grouping: Actives: Excluded	Grouping: Early Retirees: Escorted	Grouping: Early Retirees: Unescorted	FY2008 Employees: Actives	FY2008 Employees: Early Retirees	FY2008 Members: Actives	FY2008 Members: Early Retirees
80021	CERS - CITY GOVERNMENTS				X		5,771		9,834
80022	CERS - COUNTY GOVERNMENTS				X		2,492		3,534
80023	CERS - SHERRIFFS OFFICES				X		173		298
80024	CERS - AREA DEVELOPMENT				X		61		74
80025	CERS - LOCAL SCHOOL DISTRICTS				X		3,423		3,884
80030	KY RETIREMENT SYSTEMS SPRS			X			564		1,056
81000	KCTCS RETIREES	X				21		23	
85000	KY TEACHER RETIREMENT			X			9,522		12,493
85010	KTRS LOCAL SCHOOL DISTRICTS			X			5,846		6,876
85020	KTRS REGIONAL UNIVERSITIES				X		143		178
86000	JUDICIAL RETIREMENT SYSTEM			X			107		203
87000	LEGISLATIVE RETIREMENT SYSTEM			X			31		50
88000	BOARD OF BAR EXAMINERS	X				3		3	
89000	TEACHERS RETIREMENT SYSTEM	X				69		121	
90002	ALLEN COUNTY HEALTH DEPT	X				13		21	
90003	ANDERSON COUNTY HEALTH DEPT	X				8		14	
90009	BOURBON COUNTY HEALTH DEPT	X				19		37	
90011	BOYLE COUNTY HEALTH DEPT	X				11		18	
90012	BRACKEN COUNTY HEALTH DEPT	X				8		15	
90013	BREATHITT COUNTY HEALTH DEPT	X				38		62	
90014	BRECKINRIDGE CTY HEALTH DEPT	X				11		21	
90015	BULLITT COUNTY HEALTH DEPT	X				22		32	
90024	CHRISITAN COUNTY HEALTH DEPT	X				32		52	
90025	CLARK CCOUNTY HEALTH DEPT	X				44		71	
90033	ESTILL COUNTY HEALTH DEPT	X				14		20	
90035	FLEMING COUNTY HEALTH DEPT	X				10		19	
90036	FLOYD COUNTY HEALTH DEPT	X				34		51	
90037	FRANKLIN COUNTY HEALTH DEPT	X				57		98	
90040	GARRARD COUNTY HEALTH DEPT	X				12		27	
90045	GREENUP COUNTY HEALTH DEPT	X				15		16	
90054	HOPKINS COUNTY HEALTH DEPT	X				36		62	
90057	JESSAMINE COUNTY HEALTH DEPT	X				20		27	
90058	JOHNSON COUNTY HEALTH DEPT	X				49		84	
90061	KNOX COUNTY HEALTH DEPT	X				55		92	
90063	LAUREL COUNTY HEALTH DEPT	X				25		40	
90068	LEWIS COUNTY HEALTH DEPT	X				13		25	
90069	LINCOLN COUNTY HEALTH DEPT	X				12		12	
90076	MADISON COUNTY HEALTH DEPT	X				126		237	
90077	MAGOFFIN COUNTY HEALTH DEPT	X				22		33	
90079	MARSHALL COUNTY HEALTH DEPT	X				26		48	
90080	MARTIN COUNTY HEALTH DEPT	X				13		20	
90084	MERCER COUNTY HEALTH DEPT	X				14		20	
90086	MONROE COUNTY HEALTH DEPT	X				11		19	

KEHP Agency Code	Agency Name	Grouping				FY2008 Employees		FY2008 Members	
		Actives		Early Retirees					
		Included	Excluded	Escorted	Unescorted	Actives	Early Retirees	Actives	Early Retirees
90087	MONTGOMERY COUNTY HEALTH DEPT	X				32		56	
90089	MUHLENBERG COUNTY HEALTH DEPT	X				23		36	
90093	OLDHAM COUNTY HEALTH DEPT	X				11		22	
90098	PIKE COUNTY HEALTH DEPT	X				46		74	
90099	POWELL COUNTY HEALTH DEPT	X				10		21	
90110	TODD COUNTY HEALTH DEPT	X				10		21	
90118	WHITLEY COUNTY HEALTH DEPT	X				74		135	
90120	WOODFORD COUNTY HEALTH DEPT	X				8		12	
90301	FIVCO DISTRICT HEALTH DEPT	X				34		46	
90302	LINCOLN TRAIL DIST	X				146		257	
90303	BARREN RIVER DIST HEALTH DEPT	X				124		204	
90304	PURCHASE DIST HEALTH DEPT	X				138		240	
90305	NORTH CENTRAL DIST HEALTH DEPT	X				39		64	
90309	LK CUMBERLAND DIST HEALTH DEPT	X				188		358	
90310	NORTHERN KY IND DIST HLTH DEPT	X				107		173	
90311	LITTLE SANDY DIST HEALTH DEPT	X				19		38	
90312	KY RIVER DIST HEALTH DEPT	X				163		267	
90313	CUMBERLAND VALLEY DIST HLTH	X				198		330	
90314	GREEN RIVER DIST HEALTH DEPT	X				178		273	
90315	WEDCO DIST HEALTH DEPT	X				72		124	
90316	GATEWAY DIST HEALTH DEPT	X				75		133	
90317	THREE RIVERS DIST HEALTH DEPT	X				39		77	
90318	PENNYRILE DIST HEALTH DEPT	X				30		54	
90321	BUFFALO DIST HEALTH DEPT	X				19		31	
90322	LAWRENCE COUNTY HEALTH DEPT	X				14		23	
91000	KY EMPLOYERS MUTUAL INSURANCE	X				149		279	
92000	KY HIGHER ED STUDENT LOAN CORP	X				280		487	
93000	KENTUCKY HOUSING CORPORATION	X				225		379	
95000	TURNPIKE AUTHORITY	X				2		4	
95003	PERSONAL SERV CONTRACT PEOPLE	X				3		6	
95010	CHILD WATCH ADVOCACY CENTER	X				3		5	
95020	RAPE VICTIM SERVICES INC	X				7		14	
95030	OBORO AREA SHLTR & INFO SERV	X				21		32	
95040	BARREN RIVER CHILD ADVOC CTR	X				3		3	
95070	SPRINGHAVEN INC	X				8		10	
95090	GATEWAY CHILDRENS ADVOC CTR	X				2		2	
95120	KENTUCKY BAR ASSOCIATION	X				34		54	
96000	KY EDUCATIONAL TV FOUNDATION	X				50		82	
96040	DAVIESS COUNTY COMMS OFFICE	X				3		4	
96050	GATEWAY AREA DEV DISTRICT	X				15		37	
96060	KY COUNCIL AREA DEV DISTRICTS		X			1		1	

KEHP Agency Code	Agency Name	Grouping: Actives – Included	Grouping: Actives – Excluded	Grouping: Early Retirees – Escorted	Grouping: Early Retirees – Unescorted	FY2008 Employees: Actives	FY2008 Employees: Early Retirees	FY2008 Members: Actives	FY2008 Members: Early Retirees
96070	LAKE CUMBERLAND AREA DEV DIST		X			41		93	
96080	LYON COUNTY FISCAL COURT		X			20		36	
96090	PAUL SAWYER PUBLIC LIBRARY		X			15		21	
96120	HANCOCK COUNTY PUBLIC LIBRARY	X				4		5	
96130	KY CNTY JUDGE EXEC ASSOCIATION		X			1		4	
96160	BALRD CARLISLE LVNGSTN PUB LIB	X				1		1	
96180	MARSHALL CNTY REFUSE DISP DIST		X			17		33	
96190	MARSHALL COUNTY FISCAL COURT		X			147		290	
96200	HOUSING AUTHORITY GREENSBURG	X				5		5	
96210	HARDIN COUNTY SHERIFFS OFFICE		X			19		31	
96220	MCCRACKEN CO PUBLIC LIBRARY	X				13		21	
96230	MCCRACKEN COUNTY FISCAL COURT		X			133		277	
96235	MCCRACKEN COUNTY CLERKS OFFICE	X				25		53	
96240	CITY OF BARDWELL		X			8		18	
96250	THREE FORKS REGIONAL JAIL		X			25		28	
96260	NORTH MARSHALL WATER BOARD	X				8		14	
96270	CITY OF FULTON	X				41		60	
96280	SOUTH ANDERSON WATER DISTRICT	X				5		5	
96290	HOUSING AUTHORITY OF PADUCAH		X			15		34	
96300	BRECKINRIDGE CO PUBLIC LIBRARY	X				7		7	
96310	KYANNA REG PLAN & DEV AGENCY		X			50		86	
96315	JOHN L STREET LIBRARY	X				2		5	
96320	PURCHASE AREA DEVELOPMENT DIST		X			56		96	
96340	BLUEGRASS AREA DEV DISTRICT		X			51		81	
96345	LOGAN TODD REG WATER COMMISSIO		X			9		9	
96365	BIG SANDY AREA DEV DISTRICT		X			66		95	
96370	KY RIVER AREA DEV DISTRICT		X			19		33	
96385	BUFFALO TRACE AREA DEV DISTRIC		X			18		31	
96395	HARDIN COUNTY CLERKS OFFICE	X				33		52	
96400	ROWAN COUNTY PUBLIC LIBRARY	X				5		5	
96405	OFFICE OF KY LEGAL SERVICES PR	X				3		4	
96410	CITY OF PEMBROKE		X			2		2	
96415	NORTHERN KY LEGAL AID SOCIETY		X			36		67	
96420	LEE COUNTY CONSERVATION DIS	X				1		1	
96425	KENTUCKY LEGAL AID		X			17		29	
96435	CITY OF ELKHORN CITY	X				8		8	
96440	APPLACHIAN RES & DEF FUND KY		X			51		81	
96445	FLEMING COUNTY EMS	X				7		9	
96450	FRONTIER HOUSING INC	X				16		42	
96465	LOW INC HOUSING OF EASTERN KY	X				3		3	

KEHP Agency Code	Agency Name	Grouping: Actives – Included	Grouping: Actives – Excluded	Grouping: Early Retirees – Escorted	Grouping: Early Retirees – Unescorted	FY2008 Employees – Actives	FY2008 Employees – Early Retirees	FY2008 Members – Actives	FY2008 Members – Early Retirees
96475	HOUSING AUTHORITY OF MAYFIELD	X				16		25	
96485	MARION COUNTY WATER DISTRICT	X				5		12	
96490	MORGANFIELD HOUSING AUTHORITY		X			2		2	
96500	SIMPSONVILLE RURAL FIRE PROT	X				2		2	
96510	CITY OF IRVINGTON		X			9		14	
96520	LEDBETTER WATER DISTRICT	X				3		8	
96525	HSING ORIENTED MIN EST FOR SER	X				13		34	
96530	COMMUNITY HOUSING INC	X				6		7	
96535	PIKE CO SR CITIZENS PROG INC		X			6		6	
96540	WHITLEY COUNTY WATER DISTRICT	X				7		7	
96545	BREATHITT COUNTY FISCAL COURT		X			44		55	
96550	GATEWAY COMMUNITY SERVICES ORG		X			81		92	
96551	RUSSELL COUNTY DISPATCH	X				5		5	
96552	CITY OF NORTONVILLE	X				7		17	
96553	MENIFEE COUNTY PUBLIC LIBRARY	X				2		2	
96555	CITY OF OWENTON	X				6		11	
96557	HART COUNTY AMBULANCE SERVICE	X				10		18	
96561	HOUSING AUTHORITY OF OWENTON	X				1		1	
96562	LIVINGSTON COUNTY FISCAL COURT		X			43		87	
96564	KNOX COUNTY UTILITY COMMISSION	X				8		20	
96566	LEWIS COUNTY LIBRARY	X				1		1	
96567	PENNYRILE EMERGENCY ASST CNTR	X				5		5	
96568	CITY OF SCIENCE HILL	X				2		2	
96569	CITY OF LEWISBURG	X				6		10	
96570	KY ASOC SEXUAL ASSAULT PRG INC	X				3		6	
96571	HOPE HARBOR INC.	X				8		8	
96572	CUMBERLAND VALL CHILD ADV	X				2		3	
96573	HART COUNTY FISCAL COURT		X			51		64	
96575	LEGAL AID SOCIETY		X			40		64	
96577	WOMEN AWARE INC	X				11		14	
96579	KY DOMESTIC VIOLENCE ASSO	X				5		10	
96580	LK CUMBERLAND CHILDRS ADV		X			2		5	
96581	PENNYRILE CHLDS ADV CT	X				0		1	
96582	CITY OF BEATTYVILLE		X			28		48	
96583	PADUCAH POWER SYSTEM		X			54		148	
96585	HOUSING AUTHORITY OF COLUMBIA	X				4		4	
96586	CITY OF MOUNT VERNON		X			21		36	
96587	CITY OF BROOKSVILLE	X				6		10	
96589	CITY OF HICKMAN		X			17		21	
96590	CITY OF STANFORD		X			11		25	

KEHP Agency Code	Agency Name	Grouping				FY2008 Employees		FY2008 Members	
		Actives		Early Retirees					
		Included	Excluded	Escorted	Unescorted	Actives	Early Retirees	Actives	Early Retirees
96591	LIFESKILLS INC	X				1		1	
96592	CITY OF HARLAN	X				27		37	
96594	HOUSING AUTHORITY OF BENTON	X				4		11	
96595	HART COUNTY SOLID WASTE		X			13		14	
96596	CITY OF GREENSBURG		X			27		33	
96598	CITY OF ALBANY	X				37		44	
96599	ZONETON FIRE DISTRICT	X				8		17	
96600	GRTR FLEMING COUNTY WATER COM	X				2		2	
96601	WEBSTER CNTY CONSERVATION DST	X				1		1	
96602	CITY OF EMINENCE		X			11		29	
96603	BETHANY HOUSE	X				12		28	
96604	WOLFE COUNTY CONSERVATION DIST	X				1		1	
96605	CITY OF PIONEER VILLAGE	X				6		6	
96606	WOODFORD CO ECON DEV AUTHTY	X				1		1	
96607	HICKMAN URBN RENEWAL CMTY DEV	X				1		1	
96610	LIFESKILLS INC.	X				346		558	
96615	BOONE COUNTY PUBLIC LIB		X			51		66	
96616	HARRODSBURG.MERCER CO PLANNING	X				3		3	
96618	KY RIVER REGIONAL JAIL	X				2		3	
96619	HOUSING AUTHORITY OF CORBIN	X				10		21	
96620	SHELBY CO FISCAL COURT		X			119		224	
96621	BOYD CO EMERGENCY AMBULANC SVC	X				19		47	
96622	MT WASHINGTON FIRE PROTECT DT	X				13		18	
96623	KENTON CO MASTER COMMISSIONER	X				3		5	
96624	CAMPBELLSVILE-TAYLOR CO INDUST	X				1		4	
96625	CITY OF MORGANFIELD		X			48		135	
96626	CAMPBELL CO FIRE DISTRICT #1	X				7		13	
96627	CITY OF SMITHS GROVE	X				2		2	
96628	MASTER COMM FAYETTE CO CIRCUIT	X				3		4	
96629	SHELBYVILLE/SHELBY CO PKS & RE	X				7		13	
96630	BOONE CO MSTR COMMISSIONER OFF	X				1		1	
96633	SOUTHERN CAMPBELL FIRE DIST	X				2		2	
96634	HOUSING AUTHORITY OF ASHLAND	X				11		12	
96635	HOPKINSVSILLE SOLID WASTE AUTH	X				47		57	
96636	CANNONSBURG FIRE DEPT	X				2		6	
96637	WESTERN FLEMING CO WATER DIST	X				5		5	
96638	JEFFERSON CO MSTR COMM OFFICE	X				14		21	
96639	AGENCY NAME NOT IDENTIFIED	X				1		1	

KEHP Agency Code	Agency Name	Grouping: Actives: Included	Grouping: Actives: Excluded	Grouping: Early Retirees: Escorted	Grouping: Early Retirees: Unescorted	FY2008 Employees: Actives	FY2008 Employees: Early Retirees	FY2008 Members: Actives	FY2008 Members: Early Retirees
96640	HOPKINSVSILLE CHRISTIAN CO EOC		X			13		14	
96641	BUFFALO TRACE CHILDREN ADV CTR	X				2		2	
96642	RPSCC-BOYD CO 911	X				17		41	
96643	HENDERSON CO WATER DISTRICT		X			10		24	
96644	CITY OF LUDLOW		X			7		13	
96645	BOYD CO DISASTER & EMRGNCY SER		X			2		8	
96646	PIKE COUNTY PUBLIC LIBRARY		X			19		24	
96647	OWEN CO FISCAL COURT		X			33		41	
96648	BOONE CO IV D CHILD SUPPORT PR	X				7		13	
96649	AGENCY NAME NOT IDENTIFIED	X				3		6	
96651	AGENCY NAME NOT IDENTIFIED	X				22		25	
96652	HOPKINS CO ATTORNEYS OFFICE	X				6		9	
96653	AGENCY NAME NOT IDENTIFIED	X				1		1	
96654	FULTON CO FISCAL COURT		X			26		30	
96655	AGENCY NAME NOT IDENTIFIED	X				1		1	
96656	BUTLER CO AMBULANCE SERVICE	X				4		7	
96659	AGENCY NAME NOT IDENTIFIED	X				0		1	
96662	AGENCY NAME NOT IDENTIFIED	X				1		1	
96663	AGENCY NAME NOT IDENTIFIED	X				1		1	
	NO AGENCY CODE ASSIGNED			X			16		60

Totals	Total Actives - Included	X				42,747		72,893	
	Total Actives - Excluded		X			68,479		119,094	
	Total Actives					111,226		191,987	
	Escorted Retirees			X			29,128		38,306
	Unescorted Retirees				X		12,192		17,978
	Total Retirees						41,320		56,284
	Grand Total (Actives & Retirees)					152,546		248,271	

Appendix V

Analsyis of IRS & Fiduciary Considerations

KRS Legal Consultants

Ice Miller

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LEGAL COUNSEL

October 23, 2008

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Via Electronic Mail

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Executive Director
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Re: Critical Issues in Plan Transfers

Dear Mike:

Enclosed please find a chart regarding Critical Issues in Plan Transfers. Please call if you have questions.

Very truly yours,

ICE MILLER LLP

Mary Beth Braitman

Mary Beth Braitman

Terry A M Mumford

Terry A.M. Mumford

jls
Enclosure

CRITICAL ISSUES IN PLAN TRANSFERS
FOR KENTUCKY RETIREMENT SYSTEMS REGARDING SPIN-OFFS FROM CERS

The following chart is intended to outline the key considerations in the context of plan transfer situations which may arise if there is legislation to create a new Local Government Employees Retirement System (LGERS) or a new School Board Employee Retirement System (SBERS) and to provide for the transfer of members to the new LGERS or SBERS from CERS, along with a transfer of assets and liabilities.

	Qualified Plan Spin-off Issues
Can a governmental plan "spin-off" assets and liabilities associated with a defined group of members to another governmental plan?	Yes. However, there are no clear, current regulations on this point. The Internal Revenue Code ("Code") provisions dealing with private sector plans – Code Section 414(l) are not directly applicable to governmental plans. However, those provisions, particularly in conceptual terms as proposed to technical details, can be followed as a model. There is some pre-ERISA law which suggests some of the concepts would be significant today for a non-ERISA plan. We discuss some of those in more detail below.
How can the exclusive benefit rule be satisfied in a spin-off?	Code Section 401(a)(2) requires that qualified plan assets be used exclusively for plan participants and their beneficiaries – this is referred to as "the exclusive benefit rule." We have found that use pre-ERISA rules, along with the 414(l) concepts, can give much comfort that the asset transfer can be supported under the exclusive benefit rule. From a fiduciary standpoint, the exclusive benefit rule must also be balanced with the rule requiring impartiality among groups of beneficiaries.
What would 414(l) (the private sector model) require for a spin-off?	With respect to participants, 414(l) provides that participants must "receive a benefit immediately after the … transfer which is equal to or greater than the benefit he would have been entitled to receive immediately before the … transfer (if the plan had then terminated)" in order for the qualified plan to remain qualified. This concept would be satisfied in a spin-off from CERS if a participant's benefits pre-spin-off and post-spin-off are the same.

Prepared by Ice Miller LLP
October 23, 2008

	With respect to the transfer of plan assets, 414(l) requires that excess assets be allocated in accordance with a specified formula to the spun-off plan. Applying this concept in a situation where there is not full funding (or excess funding) is challenging. Actuarial analysis would be necessary to determine what is the appropriate allocation of assets and liabilities in a spin-off from CERS. Applying these concepts to a governmental plan spin-off assists in fulfilling the requirements of both the exclusive benefit rule and the fiduciary rule of impartiality.
What other precedents are available?	One approach (in addition to using Code Section 414(l)) as a model) would be to follow the IRS guidance on transfers between qualified plans. Revenue Ruling 67-213 allows transfers between qualified plans (in the ruling, from a qualified pension plan to a qualified stock bonus plan). However, as a prerequisite, the plans at issue must permit the transfer.
Would the IRS treat the spin-off as creating a partial plan termination within CERS termination?	If the IRS treated the spin-off as a plan termination, then pre-ERISA guidance would required that a governmental plan must provide for 100% vesting of accrued benefits if there is a partial or complete termination of the plan, or complete discontinuance of contributions, but only to the extent that benefits are funded. Code § 401(a)(7)(1974). Thus, if a total or partial plan termination is involved, there are two primary issues: • Affected participants must be fully vested in their accrued benefit, to the extent funded • Generally, a terminating plan must distribute benefits (but see frozen plans discussion below)—thus, depending on the form of benefit, participants would have the option of receiving the benefit or rolling it over to an IRA or eligible retirement plan, which may include the other qualified plan at issue, if it accepts rollovers. We realize this may be a very undesirable consequence in the situation at hand. The question of whether there has been a partial termination is determined on the basis of all facts and circumstances. Treas. Reg. § 1.401-6(b)(1). This Treasury Regulation defines "termination" as follows:

> For purposes of this section, the term "termination" includes both a partial termination and a complete termination of a plan. Whether or not a partial termination of a qualified plan occurs when a group of employees who have been covered by the plan are subsequently excluded from such coverage either by reason of an amendment to the plan, or by reason of being discharged by the employer, will be determined on the basis of all the facts and circumstances. Similarly, whether or not a partial termination occurs when benefits or employer contributions are reduced, or the eligibility or vesting requirements under the plan are made less liberal, will be determined on the basis of all the facts and circumstances. However, if a partial termination of a qualified plan occurs, the provisions of section 401(a)(7) and this section apply only to the part of the plan that is terminated.

Treas. Reg. § 1.401-6(b)(2).

In considering the appropriate facts and circumstances to be considered in the case of a partial termination, Internal Revenue Manual Section 7.12.1.2.7 notes the following:

- When the accrual of benefits or the rate of employer contributions is reduced, or the eligibility or vesting requirements under the plan are made more restrictive, facts and other circumstances, other than the mere fact that benefits, contributions, etc. have been cut back, enter into the determination of whether there has been a partial termination.
- While not directly applicable to governmental plans, the Section 411 Regulations provide that, where a defined benefit plan ceases or reduces future accruals, a partial termination shall be deemed to occur if the result is that a potential reversion to the employer is created or increased. A partial termination could occur because of factors other than such cessation or decrease, such as a reduction in plan participation.
- The exclusion of a group of employees previously covered by the plan, either by reason of a plan amendment or severance of employment initiated by the employer.

<u>Comparable Plan</u>. Treas. Reg. § 1.401-6(b)(1) provides that "a plan is not terminated, for example, merely because an employer consolidates or replaces that plan with a comparable plan." The Regulation refers to Treas. Reg. § 1.381(c)(11)-1(d)(4) for the definition of a comparable

	plan, as well as any additional Treasury guidance. Treas. Reg. § 1.381(c)(11)-1(d)(4) generally provides that pension and annuity plans are comparable, stock bonus and profit-sharing plans are comparable, but that profit-sharing and pension plans are not comparable. See GCM 36048. In Revenue Ruling 67-213, the Service found that a transfer from a pension plan to a stock bonus plan was not a transfer between comparable plans, treating the pension plan as a terminated plan. The Ruling provided the following discussion on comparable plans: A comparable plan is not necessarily a plan of the same type but it is one of the same category. Thus, a stock bonus plan is comparable to a profit-sharing plan and an annuity plan is comparable to a pension plan. However, as section 1.381(c)(11)-1(d)(4) of the regulations provides, if the acquiring corporation transfers the funds accumulated under a profit-sharing plan into a pension plan covering the same employees, the profit-sharing plan shall be considered terminated. Conversely, if a pension plan is replaced by a stock bonus plan, the pension plan shall be considered terminated. This is so since the basic attributes of a pension plan and a stock bonus plan lie in different categories. In the case of a spin-off between two defined benefit plans, we believe that the IRS would conclude that a comparable plan is being provided and would not require vesting. Discontinuance of Contributions. The Treasury Regulations provide that a suspension of contributions under the plan, which is merely a temporary cessation of contributions by the employer, is not a complete discontinuance of contributions. However, a complete discontinuance of contributions may occur although some amounts are contributed by the employer if such amounts are not substantial enough to reflect the intent on the part of the employer to continue to maintain the plan. Treas. Reg. § 1.401-6(c)(1). For a pension plan, a suspension of contributions will not be a discontinuance if • The benefits to be paid or made available under the plan are not affected at any time by the suspension, and • The unfunded past service cost at any time (which includes the unfunded prior normal cost and unfunded interest on any unfunded cost) does not exceed the unfunded past service cost as of the date of establishment of the plan, plus any additional past service or

	supplemental costs added by amendment. <u>Frozen Plans</u>. A plan under which benefit accruals have ceased is not terminated if, after amendment is adopted to terminate plan, the plan assets are not distributed as soon as administratively feasible but rather are held in the trust, which remains in existence. Thus, if assets are not distributed as soon as administratively feasible the plan is considered a "frozen" plan, which is an ongoing plan that must continue to satisfy the requirements of Section 401(a) to remain qualified. I.R.M. Section 7.12.1.2.19; <u>See</u> Rev. Rul. 89-87, holding that a qualified plan under which benefit accruals have ceased and assets are not distributed must continue to meet the requirements of Section 401(a) to remain qualified. However, even if the plan is treated as a frozen ongoing plan, the cessation of benefit accruals may trigger the increased vesting requirements. I.R.M. 7.12.1.2.19.
What are the Code Section 415 implications?	The Final Code Section 415 Regulations provided detail on the treatment of transfers between qualified plans to address IRS concerns that funds were being transferred between plans without ever ultimately being tested in some fashion under Section 415. If a transfer is from one qualified plan to another qualified plan that are <u>not</u> aggregated, the annual benefit attributable to the transferred assets is taken into account by the transferee plan for 415(b) testing. Further, the plan transferring the benefits must count the transferred benefits for purposes of 415 testing. Treas. Reg. § 1.415(b)-1(b)(3)(i)(B). However, in the case of a participant's election to transfer from a defined benefit plan his or her benefit that is immediately distributable (e.g., the plan is terminating or a participant is otherwise eligible for distribution), the amount transferred is treated as a benefit paid under the transferring plan and as a rollover contribution not included in the annual benefit under the plan receiving the transfer. Treas. Reg. § 1.415(b)-1(b)(3)(ii). If a transferring employee is participating in two or more defined benefit plans maintained by the employer, then the employer must aggregate all defined benefit plans for purposes of testing the employee's annual benefit under Code Section 415. Treas. Reg. § 1.415(f)-1(a)(1). For transfers between defined benefit plans that <u>are</u> subject to aggregation for purposes of Code Section 415, the plan receiving the transfer includes the transferred benefits in 415 testing, and the plan sending the transfer disregards the benefits. Thus, the benefit under each plan is determined

	by taking into account the actual benefits provided under the plan after the transfer. Treas. Reg. § 1.415(b)-1(b)(3)(i)(A). A direct transfer from one qualified plan to another qualified plan is not an annual addition in the year of the transfer for 415(c) testing. Treas. Reg. §1.415(c)-1(b)(1)(iii). The Final Regulations clarified, in the case of a transfer between a defined contribution plan and defined benefit plan, that so long as the participant made a "voluntary, fully-informed" election to transfer his or her account to the defined benefit plan, the amount transferred (determined as if the transferred amount were a rollover contribution) is not included in the annual benefit under the receiving defined benefit plan. Treas. Reg. § 1.415(b)-1(b)(3)(ii). The defined benefit plan must provide a minimum benefit for each participant, whose benefits are transferred, equal to the benefit, expressed as an annuity payable at normal retirement age, that is derived solely on the basis of the amount transferred with respect to such participant. Treas. Reg. 1.411(d)-4, Q&A-3(c)(1)(v).
If transferee plan is not terminated, can the participant elect whether to transfer? Can the employer require a transfer in the case of a plan structural change, e.g., the employer ceases to participate in or offer one plan and creates a new plan?	Yes. While the participant cannot have the option to receive the benefit directly, he or she may be given the option of leaving the benefit in the existing plan or transferring it to the new plan. See Rev. Rul. 67-123; See e.g. PLR 200411046; PLR 200130057. However, if there are different rates of employee contributions or different benefits, the Service will scrutinize any election to see if it meets their new ruling position. This issue would undoubtedly delay processing of any ruling sought. As noted above, where an employer consolidates or replaces a plan with a comparable plan there is not a plan termination. Treas. Reg. § 1.401-6(b)(1). Thus, in these situations it would appear that a required transfer would be permissible—essentially, the employer is exercising its prerogative to choose the retirement plan being offered and mandating participation, and, because the plans are comparable, the employee generally should not be negatively impacted. Even in the case of transfers between non-comparable plans, it could be argued that an employer could require a transfer, although the support is not as clear. See PLR 9436051 (finding that if governmental plan otherwise meets the pre-ERISA vesting requirements, the transfer of participation and funds to another qualified plan will not result in a prohibited decrease in employees' benefits under Code Section 411, which is generally inapplicable to governmental plans). Of course, there may be State law issues with respect to the protection of benefits. Nothing in this summary attempts to deal with those issues at all.

	Overall, the majority of private letter rulings in this area appear to provide employees the option of whether to move their funds. However, in PLR 9432028 a city and union agreed to transfer all affected police officers from one qualified plan to another qualified plan, but this was in context of collectively bargained plan. PLR 9222051 also involved a non-elective transfer of assets from one qualified plan to another, but in this case the state sponsoring the transferee plan had determined that the employer at issue no longer met the statutory definition of an employer for purposes of participants in the state plan.

Must the plans obtain private letter rulings?	There is no requirement that a private letter ruling be obtained in the case of a plan-to-plan transfer. However, where circumstances would permit, it can provide significant assurance to all parties (and plans) involved. A private letter ruling is the only way to provide complete assurance that participants will not suffer unintended tax consequences, and that the plans involved have complied with all critical Code requirements. Nonetheless, there may be a variety of situations where it may not be deemed practical to obtain a private letter ruling, especially given the substantial amount of time it may take to ultimately receive a ruling from the Service. Among the factors to weigh in the consideration of whether to obtain a private letter ruling are: • Does the transfer involves unusual circumstances—for example, where the situation appears to involve a partial termination or frozen plan, or there is a question as to whether the new plan is comparable to the old plan? Is there a question of whether vesting would be required? • Are there a substantial number of participants or a substantial amount of assets involved? • Is there a question as to whether there is a partial termination? If so, clarification—through either the private letter ruling or determination letter process—would be preferable. In this situation, we would recommend filing for a private letter ruling because of the number of participants and substantial assets involved. Once a private letter ruling request was filed, we would anticipate that it would take at least a year to receive a ruling. If the plan design involved any elective features, the timing of the ruling would be longer.
Would the new plan have to file for a determination letter in Cycle C?	As a governmental plan, the new plan would generally be a Cycle C filer. However, a new plan can file "off cycle" if the opening of the new cycle is more than 2 years away. If the new plan were created next year (for example), the plan could be filed off-cycle for a determination letter. Thereafter, the new plan would be in Cycle C (starting in 2013-4). We would strongly recommend the new plan (if established) file for a determination letter. If an off-cycle filing is made, we would anticipate that it would take 18 months to receive a

	determination letter.
What would be the impact of creating a new plan on grandfathered status that currently exists?	Creating a new plan would call into question the grandfathered status of existing members under Code 401(a)(17). This is an issue that would have to be analyzed. The existing CERS plan has certain very important private letter rulings dealing with pick-ups particularly with respect to service purchases. Those rulings speak to both income taxes and employment taxes. In our view, similar rulings would likely be impossible to obtain now, given changes in the Service's ruling position. The IRS did "grandfather" those rulings so they remain indefinitely valid. However, the new plan would not likely be able to claim the grandfathered position. On a more remote position, the Service could argue that creating a new plan could call into question the viability of those rulings for the existing plans. We think that is less likely, but needed to bring it to your attention.
Would the IRS require that a separate plan be established if the goal is to have separate actuarial valuations of certain groups?	Following the model of 414(l) and pre-ERISA regulations, it would be unlikely for the IRS to require that a separate plan be established if the primary goal is simply to have separate actuarial valuations of certain groups of employers and employees. On the other hand, if the assets of a particular group of employers (or employees) must be kept separate from other employers (or employees), the IRS would likely conclude that a separate plan and trust would be necessary. Separateness in this situation is determined by whether the assets are available to pay benefits regardless of employer (or employee group).
Would the establishment of a spin-off plan and trust require the establishment of a separate account for investment purposes?	If the spin-off plan is a qualified plan, then the trust assets may be commingled for investment purposes in a common or group trust under Code Section 401(a)(24). A new LGERS or SBERS could be handled in the same manner as CERS is handled for investment purposes.

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CIRCULAR 230 DISCLOSURE: Except to the extent that this advice concerns the qualification of any qualified plan, to ensure compliance with recently-enacted U.S. Treasury Department Regulations, we are now required to advise you that, unless otherwise expressly indicated, any federal tax advice contained in this communication, including any attachments, is not intended or written by us to be used, and cannot be used, by anyone for the purpose of avoiding federal tax penalties that may be imposed by the federal government or for promoting, marketing or recommending to another party any tax-related matters addressed herein.

Appendix VI

Estimates of Expenses to Divide CERS

KRS

KTRS

KENTUCKY RETIREMENT SYSTEMS
Perimeter Park West
1260 Louisville Road
Frankfort, Kentucky 40601

Kentucky Employees Retirement System
County Employees Retirement System
State Police Retirement System

Robert M. Burnside
Executive Director
Phone 502-696-8800
Fax 502-696-8822
www.kyret.com

MEMORANDUM

TO: Crit Luallen, Chair
Public Pension Working Group - CERS/LGERS Subcommittee

FROM: Mike Burnside, Executive Director
Kentucky Retirement Systems (KRS) Mike Burnside

DATE: October 23, 2008

SUBJECT: Estimate of KRS Expenses to Divide the County Employees Retirement System (CERS)

The following estimates of additional expenses are provided as a supplement to the CERS Working Group report.

Service credit audit costs:	$1 million per year for 5 years to hire outside consultant to conduct audit. This cost estimate is based on actual costs being incurred by the North Carolina Public Employees Pension System to do a service credit audit of approximately 200,000 accounts. The actuarial firm hired by NCPERS had dedicated 25 employees to the task. KRS would need to audit approximately 195,000 accounts. This would not be a recurring expense after completion of the initial study.
Annual Actuarial Valuation Costs:	It is estimated that the annual actuarial valuation costs would increase by 20%-30%, or $20,000 - $30,000. This would be a recurring annual expense.
Asset Allocation & Liability Study Costs:	It is estimated that increased costs for a separate Asset Allocation & Liability Study would be approximately $20,000 - $30,000. This cost would only be incurred every 4-5 years.
Experience Study Costs:	Experience study costs would likely increase 20%-30%, which would mean an increase of $20,000-$30,000 every five years.

AN EQUAL OPPORTUNITY EMPLOYER M/F/D

Computer Programming Accounting System Costs:	Some additional costs would be incurred for computer & programming and establishing and maintaining the new accounting requirements for the separate fund. These costs would likely range from $20,000 - $40,000 for staff time initially, but would decrease after initial implementation.
Publication Costs:	Some additional costs would likely be incurred for separate publications, etc. for the group. A rough estimate of increased annual cost is $20,000 - $40,000

In the event that school board employees were transferred to Kentucky Teachers Retirement System (KTRS), KRS would likely reduce its total number of staff accordingly. However, the total staff reduction cannot be calculated with any accuracy at this point. It is also likely that KTRS will be required to hire additional staff to manage the workload associated with administering the classified school board benefits system.

TEACHERS' RETIREMENT SYSTEM
OF KENTUCKY

GARY L. HARBIN, CPA
Executive Secretary

SERVING KENTUCKY TEACHERS SINCE 1940

C. JOE HUTCHISON, MBA, CPA
Deputy Executive Secretary
Finance and Administration

ROBERT B. BARNES, JD
Deputy Executive Secretary
Operations

Memorandum

To: State Auditor Crit Luallen, Chair
Public Pension Working Group – CERS/LGERS Subcommittee

From: Beau Barnes, Deputy Executive Secretary of Operations RBB
Kentucky Teachers' Retirement System

Date: October 27, 2008

Subject: Estimate of KTRS expense if the Transfer of Classified School Board Employees to Kentucky Teachers' Retirement System should occur.

The following estimates of expenses are provided as a supplement to the CERS Working Group report.

Start-up Costs: It is estimated approximately 40 additional staff would need to be hired and trained. It is anticipated this training would take a minimum of six months prior to interaction with Classified School District members. The cost is estimated to be $941,000. Additional training would also be required for an estimated 12 to 18 month period to further develop a deep understanding of the CERS system for counselors and managers at an estimated cost of $1.4 million.

Computer Systems: Estimated costs to convert existing KRS software used to manage the accounts of Classified School District members so it can be utilized by KTRS to manage the accounts of Classified School District members is $258,000. KTRS is undergoing a change in its legacy software systems, and to further coordinate the CERS software into this new scheme is estimated to cost an additional $1.8 million to $2.3 million.

Office needs: Initial costs of providing office space and fitting those offices for approximately 40 additional staff is estimated to be $394,000.

Annual costs: The annual costs to manage the retirement needs of the transferred Classified School Board Employees is estimated to be $2.9 million in personnel costs, $159,200 in office expense and $345,800 in operating costs which would include the costs of additional actuarial services, audit services, costs of printing, etc. The costs of investments would be estimated to be approximately 6 bps or 6/100% of the amount of assets transferred. The transfer of assets would likely occur over an extended period of 18 to 24 months.

This is a preliminary analysis based primarily on information obtained from KRS and from interviews and discussions with staff of KTRS. Actual costs of these items will vary from this estimate.

Appendix VII

Responses

Kentucky Education Association

Kentucky Retired Teachers' Association

Fraternal Order of Police

3KT

Edwin Davis – Retired Police Officer

Kentucky League of Cities &
Kentucky Association of Counties

KENTUCKY EDUCATION ASSOCIATION

October 24, 2008

The Honorable Crit Luallen
Auditor of Public Accounts
Chair, CERS/LGERS Subcommittee
Kentucky Public Pension Working Group
105 Sea Hero Road, Ste. 2
Frankfort, KY 40601

Re: Comments Regarding the DRAFT report for the CERS/LGERS Subcommittee

Dear Auditor Luallen,

The Kentucky Education Association and its nearly 40,000 members would like to take this opportunity to thank you for your diligent work as chair of the CERS/LGERS Subcommitte of the Kentucky Public Pension Working Group. Throughout this process you have exhibited your professionalism in dealing with the complex issues at hand and facilitated a fair process allowing all interested parties a venue for expression of ideas and concerns.

During the development of this process it was agreed that all parties would be given the chance to respond to the draft report. In response to this opportunity KEA has reviewed the draft document and suggests the following changes to the report.

Proposed changes:

On page 7 under Options, first sentence of the second paragraph, change to read:

> The Cavanaugh Macdonald Report, using the ~~current~~ new assumptions ~~and full payment of the ARC~~ based upon the experience study for the school board/non-school board employees, shows city and county employees in the existing CERS system subsidizing school board employees in the amount of ~~$43,775, 319~~ approximately $32.6 million.

Rationale: *The report notes that Cavanaugh MacDonald opined that "...long term, the new assumptions will reflect the differences between the groups better than the current assumptions do." Moreover, the $43.8 million dollar figure is apparently based on paying the full ARC for 2008, although the report notes that "...CERS employers did not pay the full ARC because the KRS Board approved a five year phase-in of the higher ARC resulting from the implementation of GASB 43/45 accounting rules." All that being the case, it seems the $32.6 million cost using the new assumptions would be more appropriate.*

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Frankfort, KY 40601
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Internet: www.kea.org

On page 8 under General Discussion of Options, add after the third paragraph another paragraph:

> Separating the two groups lends itself to further discussion about appropriate representation of school employees on the KRS Board of Trustees. The current structure provides (under 61.645) that one trustee appointed by the Governor "shall be knowledgeable about the impact of pension requirements on local governments." School employees are a larger group than local governments *and currently do not enjoy* specific guaranteed representation on the Board of Trustees.

On page 8 under General Discussion of Options, add after the above paragraph another paragraph:

> If the two groups are rated separately, it will address the approximately $32.6 million subsidy in favor of school boards, but not the $37.2 million unescorted retiree subsidy in favor of local governments. This establishes the need for a mechanism, such as proposed in HB 103 (2003 General Assembly Regular Session) and HB 11 (2004 General Assembly Regular Session), to collect this subsidy from local government employers for reimbursement to KEHP.

On page 9 under Option 1, this language seems incomplete and in need of some clarification. This might be accomplished by replacing current language with the following:

> The parties recognize that the subsidies on the pension/health insurance contributions in CERS are offset by the subsidy for unescorted city/county employees. Since these subsidies are comparable there is little incentive to incur the disruptions.

On page 12 add as a last sentence to the final paragraph:

> Any increase in costs for school boards would occur at a time when the goals of education reform are jeopardized by inadequate funding.

After careful consideration of the options outlined throughout this process and information provided through actuarial analysis, we would point out the similar amounts of the subsidies of $32.6 million for school boards and $37.2 million for local governments. Because these subsidies offset one another, combined with the substantial expense and disruption required to separate the groups, **KEA endorses Option 1 as outlined in the DRAFT report.**

Thank you again for your diligence in this process and respect for the impact any changes to Kentucky Retirement System would have on thousands of hard working school support professionals across Kentucky.

Respectfully Submitted,

Sharron K. Oxendine

Sharron Oxendine, KEA President

3KT

Kentucky's public education advocacy team

Kentucky School Boards Association Kentucky Association of School Administrators Kentucky Association of School Superintendents

Memorandum:

To: Public Pension Working Group
County Employee Retirement Systems Subcommittee

From: 3KT
Kentucky School Boards Association
Kentucky Association of School Administrators
Kentucky Association of School Superintendents

Date: October 21, 2008

Three months ago, at the beginning of the important work of the Public Pension Working Group, our three organizations presented a unified platform to this subcommittee. We outlined our concerns, including protecting the hard-earned retirement benefits of our school's classified employees, maintaining fiscal solvency for all of the retirement systems that serve school employees, and avoiding any negative consequences for Kentucky's already financially-strapped public school systems who are responsible for the employer contribution for classified school employees. Our goals and concerns remain after the in-depth examination pursued by this subcommittee.

We applaud the subcommittee for employing professional guidance to examine the complex issues related to the benefit structures for city, county and school board employees. The results of the Cavanaugh Macdonald actuarial analysis and the PricewaterhouseCoopers report for the first time provide real numbers under which we can make an informed decision. Representatives of the school boards, the cities and the counties have known for years that material subsidies exist in both the Kentucky Employees' Health Plan (KEHP) and the County Employees Retirement System (CERS). As noted in the draft report for the CERS Subcommittee, the issue of the subsidy for unescorted retirees has been debated since at least 2001. Various studies completed since that date have all confirmed a substantial subsidy to the benefit of city and county employers who currently have the option to remove their active healthy employees from the state health insurance pool, thereby driving up costs for everyone else in the pool, including teachers and classified school employees. Further, a nearly identical subsidy has been quantified in CERS. Representatives of the school boards, cities, and counties worked for several years to try to address these dueling subsidies and even reached tentative agreement in the 2003 General Assembly. While no one can specifically divine why the legislative compromise failed to pass, two conclusions can be drawn: first, that the additional costs associated with an appropriation to cover the subsidy into the CERS was too great, and second, policy makers decided that the nearly identical subsidy amounts in the two different programs did not merit the substantial upheaval and costs associated with taking any sort of corrective action.

As clearly identified in this most recent report, splitting the assets and moving members to a different system would entail years of work, millions of dollars in precious resources, and open the state to potential liabilities with the Internal Revenue Service and potentially the Social Security Administration. Further, the recent volatility in equity markets underscores the additional risk associated with any asset division.

In sum, five years later, having identified the same issues with the same results, policy makers are faced again with the same question: do we spend extraordinary sums of money that we do not have, and time and resources for which we cannot budget, in what is essentially an academic exercise to end up with a net zero gain to anyone involved? If you fix the subsidy in CERS, you will cost school districts tens of millions of dollars, and if you fix the subsidy in the KEHP, you will cost cities and counties tens of millions of dollars. It is a zero-sum game.

Therefore, our three organizations can only support Option 1 as presented in the draft report. All other options are unacceptable to school board employers because they will shift costs onto local school districts that can least afford it.

Local school districts employ nearly 50,000 people in classified school roles. These individuals provide the backbone for our educational system. They transport our children to and from school; they provide nutritional meals to sustain them through the day. They ensure that our classrooms, playgrounds and gymnasiums are clean and safe; they assist our teachers in all phases of instruction. The teaching and learning experience during our school day could not be successful without the tireless and sometimes thankless work of our classified school employees.

If the state were to adopt any of the policies in Options 2 through 5 outlined in this report, the state would be shifting a multi-million dollar burden onto local school districts. The same local school districts that have just experienced millions of dollars in cuts for extended school students – meaning our most vulnerable students are not getting tutoring after school anymore. The same schools that have just received a multi-million dollar cut in safe school funding – meaning many schools no longer employ school resource officers to ensure a safe learning environment. The same schools that have just received a multi-million dollar cut in professional development funding – meaning our teachers are not receiving the most up- to-date continuing education. These are the same schools that have cut millions of dollars from their general fund operating budgets; a recent study completed of all 174 school districts found that 135 of them had reduced staff this year in response to these cuts – meaning 1,169 staff positions in our public schools no longer exist to serve our students, and roughly half of those positions were classified school employees. If this year's cuts resulted in almost 1200 layoffs, can you imagine the pain inflicted upon our public schools if you ask them to pick up tens of millions of dollars in additional pension costs?

The Commonwealth of Kentucky, and specifically the General Assembly, has a court-ordered constitutional responsibility to fund our public schools. It is quite possibly the most important act of our state government – to equitably and adequately provide for a system of public schools for all children. Kentucky has struggled to meet this challenge since the landmark reform act of 1990. Following an initial infusion of new resources, for over a decade, nearly every new dollar going into education has been directed towards employee benefits. Employee benefits are a crucial part of that responsibility to fund the public schools, but if any of the Options 2-5 in this draft report were implemented, you would see a tremendous resource shift in school districts that would be compelled to remove instructional resources simply for the purpose of funding a retirement benefit. How would schools do that? In most school districts, 80 percent of the budget, on average, is personnel costs. There's no fat in public school budgets. If public schools were asked to increase their contribution to the retirement systems for classified school employees, there's only one way to get the money, and that is to fire people. You will be dooming to failure Kentucky school districts that have a statutory mandate to bring all students to academic proficiency by 2014. And while as subdivisions of the state, school districts understand that budgets have leaner times and happier times, as the leaders of our public schools, we cannot endorse any proposal that disproportionately shifts a cost-burden on our schools, particularly when the advocates of that shift refuse to address the other subsidy in question relating to the unescorted retirees in the health insurance pool.

Both health insurance and retirement programs rely upon dispersing risk across a pool. The greater number of lives covered reduces the risk and burden on each participant in the pool. This was the goal when these systems were setup, and it must be the overriding public policy interest for the Commonwealth as it struggles with insurance and pension issues. If policy makers play favorites with specific interest groups, allowing them to either carve themselves out or place their employees in silos, the Commonwealth as a whole loses. If you fix one subsidy without fixing the other, you are simply "robbing Peter to pay Paul." A reminder of Kentucky's motto seems apropos at this time, "united we stand, divided we fall." We must address this issue with all of our groups at the table, and not bifurcate each other for short term gain while turning a blind eye to the consequences.

The thorough examination by this subcommittee and its consultants leads to only one logical conclusion for the greatest good – Option 1.

Kentucky League of Cities

October 24, 2008

CERS/LGERS Subcommittee
Kentucky Public Pension Working Group
State Auditor, Crit Luallen, Chair
VIA EMAIL: sally.hamilton@auditor.ky.gov

Dear Chair Luallen and Members of the Subcommittee:

This letter and attachment are for the purpose of providing commentary on behalf of the Kentucky League of Cities and the Kentucky Association of Counties and their members on the draft report of the County Employee Retirement System Subcommittee of the Kentucky Public Pension Working Group.

Kentucky's cities and counties have felt the sting of unsustainable employer contribution rates on retirement benefits for some time now. Since the 2006 GASB accounting changes, CERS employer contribution rates approved by the KRS Board of Trustees have increased nearly 42 percent for non-hazardous duty employees and 28 percent for hazardous duty employees. In FY 2007 cities and counties contributed around $185 million to CERS, approximately two-and-a-half times the total amount paid in FY 2003. The aggressive changes implemented by the KRS Board of Trustees in response to GASB have forced employer contribution rates to shockingly high levels, and those rates only promise to go higher in the immediate future in the absence of additional reforms. It was this reality that led cities and counties to be among the initial groups to call upon state leaders for meaningful retirement legislation.

The changes enacted in HB 1 during the special session signaled a bold beginning in addressing the public pension crisis. However, the legislation only provided a temporary one-year reprieve from escalating contribution rates, leaving local governments in need of more permanent rate relief. No one is more aware than local governments that there is no easy fix. Despite the recommendations of some interest groups, cities and counties cannot in good conscience continue to fund escalating costs in a broken system by raising taxes during an economic downturn or neglect or abandon the services citizens need and demand. Those options do not fix the real problem and citizens would pay both monetarily and through a loss in quality of life for this type of short-sited policy making.

The promise of an effective solution lies within the work of this subcommittee. Operating under the provisions of an inviolable contract that local governments are committed to honoring and protecting for their employees and retirees, the possibilities

Cantrill, Janet (APA)

From: Hamilton, Sally (APA)
Sent: Monday, October 20, 2008 10:57 AM
To: Cantrill, Janet (APA)
Subject: FW: DRAFT Report of the CERS Subcommittee
Importance: High

----Original Message-----
From: Haskamp, Greg (Finance Secretary's Office)
Sent: Monday, October 20, 2008 10:53 AM
To: Hamilton, Sally (APA)
Subject: FW: DRAFT Report of the CERS Subcommittee
Importance: High

From: eddavis614 [mailto:eddavis614@insightbb.com]
Sent: Saturday, October 18, 2008 9:49 PM
To: Haskamp, Greg (Finance Secretary's Office)
Subject: Re: DRAFT Report of the CERS Subcommittee

Greg Haskamp
Office of the Secretary
Finance & Administration Cabinet

Dear Sir,
After careful consideration of the five possible courses of action to address the question raised, I choose Option 1, which would leave the system "as is".This is not something that was done in haste, but was done after a lot of thought on my part, and I will attempt to explain some of my reasons for this choice.
First of all, this is not the time to create a new pension system for City & County employees such as LGERs which would require the Membership and assets to be split. There would be nothing gained by transferring a problem from one system to another, the money, assets and membership would still be the same with just a different name. The cities and counties are having hard times, but the state is also having many of the same problems with finances. The problem with the Retirement system did not happen over night and I don't expect it will be solved over night. The problems of moving from one system to another seem to be much greater than any benefit that might be gained. If there are to be changes made, we need to sure that by making these changes, we don't make a bad situation worse.

Respectfully, Edwin A. Davis (Retired Police Officer and former Trustee of the Kentucky Retirement Systems,CERS) -----

Dear Members of the CERS Subcommittee,

Attached you will find the draft report of the CERS subcommittee. Please review and direct all comments in formal letter, via email, to Sally Hamilton in the Auditor's Office Hamilton: sally.hamilton@auditor.ky.gov so that they may be appended to the final report of the subcommittee. **Comments are due by close of business, on Friday October 24th**. Appendicies, attachments and the executive summary will be presented to the subcommittee members at the next meeting

Also, please note: **The final meeting of the subcommittee will be held on Tuesday, October 28, 2008 at 2pm in room 129 of the Capitol Annex.**
Thank you,

Greg Haskamp

Office of the Secretary

Finance & Administration Cabinet

Telephone 502/564-4240

for immediate rate relief are limited. In searching for options for near-term rate relief, cities and counties have concluded that an elimination of the classified school board subsidy and the establishment of a full funding standard with a phase-in period to reach the Actuarially Required Contribution (ARC) for funding of retiree health benefits are the only viable options available to the legislature without undermining the sustainability of the retirement systems. The elimination of the school board subsidy can be accomplished in a number of ways as appropriately outlined in the options presented in the draft report.

Governor Beshear's charge to the subcommittee in his executive order was to explore two options for eliminating the school board subsidy– the creation of LGERS or separation of classified school board employees into another system. The Governor's order does not call for the examination of the unescorted retiree subsidy, which the draft report summarily concludes must be considered in any analysis of local government retirement systems. Unfortunately, the insertion of this health care cost issue serves to confuse the analysis and distracts from the discussion of retirement reform. The unescorted retiree issue was further complicated with the possible inclusion of information in the PricewaterhouseCoopers analysis that may not have reflected actual unescorted retiree data.

Since the unescorted retiree issue has been included in the report, it is worth noting that the study ignores the impact of flexible spending plan participants who opt out of active coverage in the state health plan but participate upon retirement. Moreover, the study does not recognize the unescorted retiree subsidy has already been addressed by the General Assembly. The unescorted retiree subsidy will become non-existent over time as the 2003 changes to retiree health insurance benefits take full effect. The work of this subcommittee should be more appropriately focused on the proper allocation of personnel, and assets and liabilities for retirement purposes.

The draft report provides five options to address the retirement ailments of local governments. While four of the options present a means to correct the school board subsidy shouldered by local governments, the first option is to leave the system "as is." Doing nothing is no solution and is unacceptable for local governments in the absence of other action that would curb the increase in employer contribution rates.

There is an additional option that could benefit cities, counties, and school boards - the enactment of legislation similar to the provisions of HB 1 related to the state's funding of the KERS ARC. The General Assembly could establish an extended phase-in period for reaching the full ARC and create a full-funding standard for OPEB liabilities. The KRS Board of Trustees would be required to follow this legislation for setting yearly employer contribution rates. The measure would extend the impact of rate increases over a greater length of time until 2003 health insurance changes and the HB 1 reforms have time to take greater effect. Not only could this assist cities and counties, but it could also mitigate the burden of rising retirement costs on school boards.

Kentucky League of Cities

Unlike the General Assembly, local governments have been paying their bills on time and want to continue on the prudent path toward full funding of pension benefits. Local governments acknowledge pension liabilities should be funded at 100 percent. On the other hand, there is more room for flexibility in dealing with the retiree health insurance liabilities because of the changing nature of the health care market and the eventual import of the 2003 health benefit changes. Without a change, some local governments and their employees may not be around long enough to realize the relief provided by the 2003 health benefit changes and HB 1.

The state should strive to provide more substantive changes to the retirement systems so that benefits and costs are properly allocated. Local governments realize that process may be long and unpleasant, but avoiding the problem today may only worsen it tomorrow. The notion that two unrelated subsidies "cancel" is an easy excuse for a failure to take action. If nothing is done, the subsidies are guaranteed to be revisited and reevaluated again as they each change in the coming years, especially as the effects of the 2003 health benefit reforms completely erase the argument of a "wash."

On behalf of KLC and KACo, and our membership of 390 cities and 120 counties, we would like to commend the chair of the subcommittee and its members on their professionalism and diligence over the past several months. The work of this subcommittee has helped paint a more complete picture of the retirement landscape and will hopefully serve as a basis for additional change. The future of our local governments and the Commonwealth depends on it.

Attached to this letter, please find specific comments and questions from cities and counties related to the report in its draft form.

Sincerely,

Sylvia L. Lovely

Sylvia L. Lovely
Executive Director/CEO
Kentucky League of Cities

Bob Arnold

Bob Arnold
Executive Director/CEO
Kentucky Association of Counties

Kentucky League of Cities

Questions Answered Below by KRS (Oct. 27, 2008)

QUESTIONS REGARDING THE DRAFT OF THE
PUBLIC PENSION WORKING GROUP
COUNTY EMPLOYEE RETIREMENT SYSTEM SUBCOMMITTEE
October 17, 2008

1. Page 6, Summary of Results: First and second bulleted paragraphs.

- "CERS School Board employees do have different actuarial demographics than Non-School Board Employees. School Board Employees:
  - Terminate earlier;
  - Retire later;
  - Have a different mortality rate; and **[Is the mortality rate higher or lower?]** NSB females on the average have one year shorter lifespan that SB females
  - Have significantly lower average salaries; ($17,592 versus $33,662 for NSB)"

- "When rated separately:
  - Non-School Board employees actually receive a small subsidy from school board employers on pension contributions.**[How small is the subsidy?]** 0.43% of payroll
  - School Boards receive a larger subsidy from non-school board employers on the health insurance contributions" **[How much larger is the subsidy? The Cavanaugh study said the subsidy was a "material" subsidy?]** 2.88% of payroll

2. Page 7, Subcommittee Approach/Methodology, paragraph at the top of the page. **[Is the $43,775,319 subsidy in favor of the school boards the "net" subsidy? How was the subsidy calculated?] It is a net subsidy of pension and insurance combined. Look at page 5 of the Oct 9 letter from Cavanaugh. It is the sum you get when you subtrace the School board Current Assumptions from the Combined for pension and insurance, and the Non-School Board Current Assumptions from the Combined for pension and insurance.**

3. Page 7, Subcommittee Approach/Methodology, paragraph at the top of the page. The last sentence in that paragraph says: "The use of the actual ARC would result in a different subsidy amount." **[What would that subsidy be? Would it be more or less?] This is an issue raised by adding the language from Patrick Welsh. Cavanaugh computed the subsidy on the full calculated value of the ARC. CERS is actually paying a reduced amount due to a five-year phase in to full health insurance contributions adopted by the Board. Patrick's assertion is that it would be a different value, but Cavanaugh has not verified Patrick's numbers.**

4. Page 7, Subcommittee Approach/Methodology, first full paragraph on page. The first sentence in that paragraph says: "Using the new assumptions based on the experience study for the school board/non-school board employees, Cavanaugh MacDonald found a subsidy of approximately $32.6 million." **[The $32.6 million did not appear in any of the previous documents relating to the Cavanaugh study." Where did this number come from and why is it different form the $43.8 million subsidy mentioned in 3. above?]**
This came from a Oct 9 email from Cavanaugh to Bill Thielen. Cavanaugh was asked to look at the subsidy using the actual payroll data from 2007-2008 instead of projected for 2008-2009. The lower number comes from the actual payroll data from last year to have an apples-to-apples comparison with the report from PriceWaterhouse. We did not ask for an updated letter to this effect. I can forward the email to you.

5. Page 7-8. Options, last paragraph on page 7 and top of page 8. The last sentence in the paragraph states: "The PwC study has incorporated to the extent possible recommendations from the Kentucky League of Cities of affected agencies." **[To what extent was the Kentucky League of Cities recommendation used. It does not appear that the subsidy amount for unescorted retirees changed at all. How was the data provided by the League utilized? Why were the issues raised by the League of Cities and KACO not addressed in the draft report?] This is a Personnel Cabinet and PWC question.**

6. Page 8, General Discussion of Options, fourth full paragraph on page. This paragraph states: "If school board employees are to be rated separately from city and county employees, the only alternative is to divide both the membership and the assets into two separate groups, regardless of the governance structure." **[This statement would not be true if we leave existing CERS employees in the current retirement plan, and deal with new hires differently.] KRS has had numerous discussions with KLC and KACO on this issue. If you close CERS to new employees and place new employees in a different system, Cavanaugh advises that you have to use a different actuarial method. You must go from funding on a percent of payroll to funding on a level dollar amount, which will drive the cost up significantly from what they are paying today. This is not a viable option from KRS' standpoint.**

7. ****GENERAL COMMENT: While not addressed specifically by the subcommittee, we believe the Public Pension Working Group should be made aware that the reemployment provisions of House Bill 1 have placed local governments at a competitive disadvantage. This competitive disadvantage is exacerbated when it comes to re-employing hazardous duty retirees. If local governments wish to rehire a previously retired state or local government employee, that employee may not accrue an additional retirement annuity, even though the government must still pay the employer contribution to the retirement system as well as the cost of a single**

premium health policy. We believe local governments should be granted relief from these overly restrictive re-employment provisions.

Kentucky League of Cities

ADDENDUM
TO OCTOBER 24, 2008 LETTER
FROM THE
THE KENTUCKY LEAGUE OF CITIES (KLC) AND
THE KENTUCKY ASSOCIATION OF COUNTIES (KACO)

KLC and KACO submit the following additional comment to the CERS/LGERS Subcommittee draft report, and request that the comment be made a part of their joint October 24, 2008 response:

> KLC and KACO believe that an additional alternative exists that can provide relief from the "material" health care subsidy that Cavanaugh MacDonald says local governments are currently providing to school board employees in CERS. Under this alternative, which amounts to a clarification of Option 4, found on page 10 of the draft report, all current members of CERS, both school board and non-school board, would remain in that retirement system.
>
> At a future legislatively enacted date, newly hired classified school board employees would enter the Kentucky Employees Retirement System or other appropriate retirement system. New city and county employees would continue to become members of CERS. It is submitted, that this option would not require the splitting of assets, nor would it require that the membership of CERS be split. It would also allow employer contributions to continue to be calculated as a percentage of payroll and would not require level dollar funding.
>
> The treatment of newly hired school board employees would be completely consistent with the way health benefits for new hires were changed with the enactment of legislation in 2003.

KLC and KACO wish to express their appreciation to the chair and members of the subcommittee for their willingness to consider this alternative. While it is acknowledged that dealing with this retirement issue is very complex, it is nevertheless believed that the modification outlined above should be given careful consideration as a viable alternative for dealing with the CERS subsidy.

Sincerely,

Sylvia L. Lovely

Sylvia L. Lovely
Executive Director/CEO
Kentucky League of Cities

Bob Arnold

Bob Arnold
Executive Director/CEO
Kentucky Association of Counties